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# **NAVAL POSTGRADUATE SCHOOL**

**MONTEREY, CALIFORNIA**

## **THESIS**

**IRANIAN SANCTIONS: AN ACTOR-CENTRIC ANALYSIS**

by

Andrew G. Plumer

March 2012

Thesis Co-Advisors:

Robert Springborg  
Robert Looney

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**IRANIAN SANCTIONS: AN ACTOR-CENTRIC ANALYSIS**

Andrew G. Plumer  
Lieutenant Commander, United States Navy  
B.S., Kansas State University, 1999

Submitted in partial fulfillment of the  
requirements for the degree of

**MASTER OF ARTS IN SECURITY STUDIES  
(MIDDLE EAST, SOUTH ASIA AND SUB-SAHARAN AFRICA)**

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March 2012**

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## **ABSTRACT**

Economic sanctions concerning Iran's nuclear program are not having their intended political effect. Uranium enrichment continues, despite sanctions. This thesis argues that international economic "smart" sanctions are failing because they are not altering the relative positions of power between the factional actors in the Iranian political economy, and because the actors who desire to continue enrichment remain in control of the economy and state institutions. The Iranian political economy is a clientelistic state, with differing rival autonomous patron-actors, and associated client bases, all competing for a larger slice of economic rents. Economic sanctions have failed because the more conservative actors and their clients have entrenched themselves in the economy and control of these rents, thereby diverting the costs of sanctions to their political competitors, while simultaneously using sanctions to strengthen their own client base. Research indicates that while stronger economic sanctions could be designed, their chances of success remain unknown. Only a complete and thoroughly enforced embargo on Iranian petrochemical sales, with a simultaneous economic strengthening of reformist actors in the political economy, who are open to a nuclear enrichment policy change, will result in the political goals sanctions are designed to achieve.



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## **LIST OF ACRONYMS AND ABBREVIATIONS**

BPD	Barrels Per Day
CIA	Central Intelligence Agency
CISADA	Comprehensive Iran Sanctions, Accountability, and Divestment Act
EU	European Union
FDI	Foreign Direct Investment
GAO	Government Accountability Office
GCC	Gulf Cooperation Council
GHORB	Gharargah Sazandegi Khatam al-Anbia (Engineering firm)
GDP	Gross Domestic Product
HEU	Highly Enriched Uranium
IAEA	International Atomic Energy Agency
ICA	Islamic Coalition Association
ILSA	Iran-Libya Sanctions Act
IMF	International Monetary Fund
IRGC	Iranian Revolutionary Guard Corps
IRP	Iranian Revolutionary Party
IO	Information Operations
ISA	Iran Sanctions Act
ISI	Import Substitution Industrialization
ISP	Internet Service Provider
LEF	Law Enforcement Forces
LEU	Low Enriched Uranium

MOIS	Ministry of Intelligence and Security
NIOC	National Iranian Oil Company
NPT	Nuclear Non-Proliferation Treaty
OFAC	Office of Foreign Assets Control
OPEC	Organizations of Petroleum Exporting Countries
PRC	Peoples Republic of China
SAP	Structural Adjustment Program
U.A.E.	United Arab Emirates
UF <sub>6</sub>	Uranium Hexafluoride
UN	United Nations
UNSC	United Nations Security Council
U.S.	United States
WMD	Weapons of Mass Destruction

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# I. INTRODUCTION

## A. MAJOR RESEARCH QUESTION

The resolution of the Iranian nuclear issue remains a central obstacle for U.S. and worldwide foreign policy. Although, by now, it is likely that Iran has enough low-enriched fissile Uranium on hand to eventually develop a nuclear weapon, it still must continue enrichment to a higher grade to achieve the goal.<sup>1</sup> The legitimacy of continued enrichment will almost certainly be contested due to the numerous United Nations (UN) resolutions requiring Iran to cease this activity.<sup>2</sup> As long as a UN zero-enrichment policy remains for Iran,<sup>3</sup> the imposition of economic sanctions, diplomacy, and military containment appear to be the tools of choice by all governments to deal with and resolve the issue. Although political leaders insist that all options are on the table, including military options, this is unlikely, given the current fiscal, political, and military constraints of the day. But current economic sanctions do not appear to be changing the regime's behavior and, in fact, the regime appears to be simply digging in its heels and resisting any peaceful change in its nuclear enrichment policy (among other policies).

Currently, there are no standard methods of assessing the effects of Iranian sanctions, which, itself, is a difficult and politicized effort among governments. Assessments of effectiveness vary depending upon which political or economic goal is being measured for each sanctions regime.<sup>4</sup> If there is consistency among governments, especially among UN members, it is that sanctions are not working vis-à-vis the Iranian nuclear issue.<sup>5</sup> Recent announcements about sanctions' effects against the Iranian

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<sup>1</sup> Mark Fitzpatrick, "Iran: The Fragile Promise of the Fuel-Swap Plan," *Survival* 52, no. 3 (June 2010), 72. doi:10.1080/00396338.2010.494878.

<sup>2</sup> Mark Fitzpatrick, *The Iranian Nuclear Crisis: Avoiding Worst-Case Outcomes* International Institute for Strategic Studies (Oxford: Routledge, 2008), 15.

<sup>3</sup> *Ibid.*, 23.

<sup>4</sup> Kenneth Katzman, *Iran Sanctions*: Congressional Research Service, Library of Congress, (Washington, D.C., 2011), 48. <http://openocrs.com/document/RS20871/>.

<sup>5</sup> *Ibid.*, 48.

economy also indicate failure: “An IMF [International Monetary Fund] statement issued June 13, 2011, casts some doubt that international sanctions are seriously harming Iran’s economy.”<sup>6</sup> Academic assessments of sanctions regimes typically follow case studies (usually after the sanctions regimes have ended and all data is available), which are detailed but tenuous in their predictive capability due to the multiple variables used,<sup>7</sup> especially in ongoing cases.

Policymakers have historically used sanctions regimes to achieve certain foreign policy objectives against their target state. When used against an authoritarian state, an assumption made by these policymakers is that sanctions are best used in a way that eliminates the capabilities and/or strengths of the target state (i.e., revenues, resources), thus achieving a change in policy by default. In reality, when sanctions are used in this manner against an authoritarian or autocratic state, the success rate is low.<sup>8</sup> In the case of Iran, as an example, historic sanctions have been used to “cripple the productive base of the economy ... curtail Iran’s ability to support international terrorism or acquire sophisticated military hardware. Economic hardship and fiscal austerity would demoralize the population and turn it against the regime.”<sup>9</sup> It was hoped that the loss of popular support, resources and financing would alter the regime’s foreign policy, and this has not happened.<sup>10</sup>

The use of economic sanctions has historically come in two types: comprehensive sanctions and smart sanctions.<sup>11</sup> Comprehensive sanctions are a broad sanctions regime and usually cover a wide range of actions (boycotts, embargoes, asset freezes, travel bans). They are also unpopular (and often ineffective) due to the massive economic collateral damage caused to the civilian population, as well as the ability of the regime’s

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<sup>6</sup> Kenneth Katzman, *Iran Sanctions*: Congressional Research Service, Library of Congress, (Washington, D.C., 2011), 50. <http://opencrs.com/document/RS20871/>.

<sup>7</sup> Gary Clyde Hufbauer, *Economic Sanctions Reconsidered*, 3rd, Expanded ed. Peterson Institute for International Economics, (2007), Washington, D.C.: 55–56.

<sup>8</sup> *Ibid.*, 166.

<sup>9</sup> Jahangir Amuzegar, Adjusting to Sanctions, *Foreign Affairs* 76, no. 3 (1997), 31.

<sup>10</sup> *Ibid.*, 31.

<sup>11</sup> Hufbauer, *Economic Sanctions Reconsidered*, 138.

leadership (usually authoritarian) to stay in control by allocating the remaining scarce resources and shifting the costs of the sanctions onto the populace.<sup>12</sup> Smart sanctions (i.e., targeted sanctions or designer sanctions) are an alternative sanctions regime, the use of which is relatively new internationally. Smart sanctions attempt to achieve a foreign policy goal with a very narrow sanctions regime by minimizing the economic collateral damage to the population and general economy and targeting “specific officials or government functions.”<sup>13</sup> Examples include: the freezing of a specific asset or assets used by the regime leadership; a ban on specific exports to the target state; the suspension of aid, or; banning travel for certain regime officials.<sup>14</sup> Their humanitarian sentiment notwithstanding, these sanctions do not have a good track record against autocratic regimes such as Iran,<sup>15</sup> and are better as a “signaling device than as a coercive measure.”<sup>16</sup> Smart sanctions are “not a magic bullet for achieving policy goals,”<sup>17</sup> as there are many variables for failure. Often, in the case of authoritarian regimes, sanctions are sidestepped with black markets or diverted so that internal power rivals absorb the costs. In some cases, they require too high a level (and length) of international participation and administration before seeing results, or are simply ignored altogether by the regime—like Iran, which is actively taking measures to withstand economic sanctions.<sup>18</sup> The net result in these cases of failure is that the underlying political-economic structure of the target state is not changed. The regime leadership targeted for the specific policy change remains in political and economic control of the state and, therefore, refuses the intended change in policy. A new approach is therefore needed.

This thesis will propose a new method of assessing current Iranian smart sanctions regimes, specifically analyzing the effectiveness of the sanctions regime against

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<sup>12</sup> Hufbauer, *Economic Sanctions Reconsidered*, 138.

<sup>13</sup> Ibid.

<sup>14</sup> Ibid.

<sup>15</sup> Ibid., 167–169.

<sup>16</sup> Ibid., 139.

<sup>17</sup> Ibid., 141.

<sup>18</sup> Jahangir Amuzegar, Sanctioning the Islamic Republic: A New Global Wave, *Middle East Economic Survey* (27 December 2010), 3–4.

political actors in Iran. This new approach will recognize that while Iran is an authoritarian state, it has factionalized elite (versus a highly concentrated elite, as in Hussein's Iraq) with multiple actors who have differing voices in policy. The use of smart or targeted sanctions against the correct actors could result in a change in the structure of the political-economy, leading to a policy change. Research will take the form of an actor-centered approach and look at the key actors (factions, clients, and institutions under their control) in the Iranian political economy, identify how sanctions affect their interests, attempt to determine what the effects on the overall Iranian political economy are, as well as recommend a new sanction regime better tailored to take these interactions into effect. The Iranian economy, as will be shown in subsequent chapters, is overly reliant upon its petrochemical sales, which generate 20 percent of its \$870 billion Gross Domestic Product (GDP), and accounting for 80 percent of government revenues.<sup>19</sup> The actors and their intermediaries involved at the top of this political economy—the Shiite clerics and the security forces—have both been specifically targeted in the various iterations of sanctions currently on the books, but it appears that these sanctions are still failing to alter Iranian policy. This thesis will address the following questions: Who are the key actors in the Iranian political economy? What are their interests? How do these actors interact with one another (i.e., does the structural power of capital exclude some actors from having a full voice in state policy)? What are possible changes in these actors' utility schedules likely to have on overall policy decisions? How might targeted sanctions differently impact these actors? If these actors' interests are impacted, could that be translated into a change in policy, specifically the nuclear policy? Can economic sanctions be selectively targeted to this level?

This thesis will recommend alternative levels of sanctions and/or other foreign policy or diplomatic options to influence key actors within the Iranian political economy who have a voice in Iranian state policy. Economic and diplomatic actions by third parties (third countries, institutional actors, the UN) will also be assessed when gauging the appropriate policy recommendations. This thesis will also assess the actual worldwide potential for a successful implementation of such actions, as the political appetite by each

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<sup>19</sup> Katzman, *Iran Sanctions*, 6.

individual actor to participate in collective action, may not exist. In its conclusion, this thesis will present the authors recommended options for success given the worldwide political and economic constraints.

## **B. IMPORTANCE**

Resolving the Iranian nuclear issue is of the highest importance to U.S. and worldwide security. Iran's Islamist/revolutionary sentiment, strategic location alongside vital energy shipping lanes, large supply of energy reserves and potential for interfering or disrupting its neighbors (who happen to be key U.S. allies) can turn a tactical miscalculation into strategic failure. Iran's history of interference in its neighbors' affairs, and its continued sponsorship of terrorist organizations, also makes the handling of diplomatic overtures or punitive economic sanctions a delicate issue.

Economic sanctions appear to be the tool of choice to deter and alter Iranian behavior, specifically the Iranian nuclear enrichment issue. However, material gathered to support this thesis indicates that no academic or governmental consensus exists as to the exact types of sanctions (and associated diplomatic actions) that are required to achieve the political effect desired (i.e., the cessation of nuclear enrichment). Excellent assessments of the current state of the Iranian economy are available and key institutional actors in critical sectors of the Iranian economy can be identified. Yet, current economic sanctions only appear to strengthen the regime's hand and deeper entrench its position, actually having the exact opposite political effect intended.

This thesis warrants research due to the widespread cases of smart sanctions' misalignments in an authoritarian political-economic model. Current sanctions regimes are designed to change the policies of a specific state through the weakening of the regimes' finances, access to resources, or legitimacy, while minimizing the effect on the population. As discussed, when used against an authoritarian state, these efforts usually fail to bring about a change in the political economy of the state. This method would have profound policy implications and could eventually lead to an academic consensus on sanctions regime recommendations against a targeted state. Concluding the research of this thesis, the most feasible recommendation of translating economic sanctions into the

political reality of coercing Iran to abandon its nuclear enrichment pursuits will be made. An Iranian change in its nuclear enrichment policy (the dependent variable) could take several forms, to include: cutting a deal with the international community to conduct Uranium enrichment offshore (as in the proposed Russian fuel rod swap) or even a complete abandonment of its enrichment program and a surrendering of all its stockpiled low-enriched Uranium. This thesis will examine whether economic sanctions can achieve these effects, based on an actor-centric approach, and what levels of economic sanctions would be required to do so.

## **C. PROBLEMS AND HYPOTHESES**

### **1. HYPOTHESIS #1: Analysis of Whether Sanctions' Effects Should Be Actor-Centric**

Certain institutions within the economy, such as the Iranian revolutionary guard corps (IRGC), have “extended their influence into virtually every sector of the Iranian market.”<sup>20</sup> Other institutions, including the foundations (bonyads), while not directly controlled by the IRGC but linked to it, and the ruling clerics, are also well integrated into the Iranian economy.<sup>21</sup> These institutions are linked to four primary actors in the Iranian political economy today—conservatives, neoconservatives, pragmatists, and reformists—who have discernible economic interests in fighting over economic rents that have allowed their growth and further expansion into other sectors of the Iranian economy, often at the expense of another. The correct applications of sanctions can impact these actors, and if impacted, there will be policy consequences that can be predicted through the use of a political economy model. Literature on current Iranian sanctions indicates that one of the main reasons sanctions are not working is because they keep foreign investment out of Iran, which allows these powerful internal actors to take over the financing and development of projects, expanding their economic clout and,

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<sup>20</sup> Frederic M. Wehrey, *The Rise of the Pasdaran* [Electronic Resource]: *Assessing the Domestic Roles of Iran's Islamic Revolutionary Guards Corps*, National Defense Research Institute (U.S.) (Santa Monica, CA: RAND, 2009), 55.

<sup>21</sup> *Ibid.*, 57.

therefore, control of policy.<sup>22</sup> The IRGC's hard-line stance on the nuclear issue also encourages sanctions, which weaken their own internal political enemies, such as are found within the wealthy reformers of the bazaar class.<sup>23</sup> A new sanctions regime must take all actors into account in the political economy and be used selectively to specifically weaken hard-line actors on the nuclear issue while promoting reformers. Such sanctions could weaken these hard-line actors enough to allow for an open dialogue in government, possibly leading to a reversal in the Iranian nuclear policy.

## **2. HYPOTHESIS #2: Sanctions Must Alter the Current Asymmetric Balance of Power in the Iranian Political Economy to Achieve Their Political Objectives**

Current literature indicates the more conservative Iranian actors control the economy and are reorganizing the economy to withstand severe economic sanctions. This reorganization is designed to keep the conservative actors in power and the nuclear enrichment program on track.<sup>24</sup> A sanctions regime that continues to keep foreign investment out also keeps entrenched institutions such as the IRGC in virtual control of the economy via expansion and seizure of development projects, while ensuring no other domestic competition emerges from other actors.<sup>25</sup> The conservatives have launched an aggressive information operations (IO) campaign to garner domestic support for the nuclear program despite potential economic hardships.<sup>26</sup> High oil prices also inhibit the effects of sanctions, as "many believe the economic effects of international sanctions can be tolerated by the regime as long as world oil prices remain high, at over \$90 a barrel in

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<sup>22</sup> Ali Alfoneh, All the Guard's Men: Iran's Silent Revolution, *World Affairs* 173, no. 3 (September/October 2010), 78.

<sup>23</sup> Ibid.

<sup>24</sup> Omid Memarian, Iran: Revolutionary Guards Tighten Economic Hold, *Global Information Network* (30 December 2009).

<sup>25</sup> Alfoneh, "All the Guard's Men: Iran's Silent Revolution," 78.

<sup>26</sup> Scott Peterson, Iran's Revolutionary Guard Tightens Grip, *The Christian Science Monitor*, 9 December 2009.



July 2011.”<sup>27</sup> Research will show how entrenched actors are vulnerable, and that competitor actors in the Iranian economy could, once in power, bring about the political objectives of the sanctions regimes.

### **3. HYPOTHESIS #3: Economic Sanctions, Diplomacy, and Military Containment are the Best Options for a Solution**

This thesis will take the starting position that economic sanctions, diplomacy, and military containment will remain the tools of choice for states seeking to solve the Iranian nuclear problem, as appetite for a third major theater war by a UN-sanctioned coalition in the Middle East is not politically or fiscally realistic. Thesis analysis will recommend alternative levels and avenues of each and assess reactions by Iranian domestic actors and leadership. Iranian political actors and their constituencies will be assessed as to the effects of an overarching sanctions regime combined with diplomatic overtures and ongoing military containment.

## **D. LITERATURE REVIEW**

### **1. Introduction**

Continuous UN and Western policy debates surround the Iranian nuclear issue and exactly what to do about it. This is especially true in the U.S., which has had a history of imposing economic sanctions since World War II, throughout the world in various and increasing forms. Economic sanctions have been applied against Iran since the 1979 Islamic revolution and have continued under successive U.S. presidents to “punish Iranian malfeasances.”<sup>28</sup> Given this history and the perceptions that existing economic sanctions toward the Iranian nuclear issue have failed, it is not surprising that as the issue intensifies and no resolution is forthcoming, more severe sanctions are the

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<sup>27</sup> Katzman, *Iran Sanctions*, 50.

<sup>28</sup> Suzanne Maloney, Sanctioning Iran: If Only it Were so Simple, *The Washington Quarterly* 33, no. 1 (January 2010), 138–139. doi:10.1080/01636600903430673.

answer.<sup>29</sup> The historic use of economic sanctions, with some successes and some failures across the world, raises questions: Who are the main actors in the Iranian economy who control policy, specifically the nuclear enrichment policy? Why are current sanctions regimes failing to influence these actors and alter this policy? How are sanctions regimes best assessed? What change in sanctions regime is required to achieve policy goals? To answer these questions, recent literature is sampled with differing opinions; some literature advocates continuing and/or expanding sanctions; some literature recommends mixing sanctions with diplomacy in a “carrot and stick” approach; other literature recommends abandoning sanctions altogether, as they will have no influence on actors. The dependent variable in this study is the change in the Iranian nuclear enrichment policy, the independent variable is the level of economic sanctions, and the intervening variables are the actors, to include Iranian domestic actors, as well as international actors.

## **2. Background**

During initial research, comparisons of current Iranian sanctions literature against past sanctions literature was attempted. These past cases, where sanctions have been applied with both unsuccessful outcomes (North Korea, capability to make nuclear weapons;<sup>30</sup> Cuba, democratization)<sup>31</sup> and successful outcomes (Libya, ending of nuclear research program;<sup>32</sup> Sudan, ending support to terrorism;<sup>33</sup> and South Africa, ending apartheid)<sup>34</sup> were reviewed. While these case studies were enlightening, more important was the discovery that the comparison of differing international sanctions campaigns with different objectives and variables is a major research gap. In other words, the political effects desired (i.e., independent variables) are often so dissimilar—there is no identified

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<sup>29</sup> Suzanne Maloney, Sanctioning Iran: If Only it Were so Simple, *The Washington Quarterly* 33, no. 1 (January 2010), 139. doi:10.1080/01636600903430673.I

<sup>30</sup> Hufbauer, *Economic Sanctions Reconsidered*, 144.

<sup>31</sup> Hossein Askari, *Case Studies of U.S. Economic Sanctions: The Chinese, Cuban, and Iranian Experience* (Westport, CT: Praeger, 2003), 157.

<sup>32</sup> Meghan L. O’Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism* (Washington, D.C: Brookings Institution Press, 2003), 205.

<sup>33</sup> Ibid., 269.

<sup>34</sup> Richard Haass, Meghan L. O’Sullivan, *Honey and Vinegar: Incentives, Sanctions, and Foreign Policy* (Washington, D.C: Brookings Institution Press, 2000), 95.

common way to compare the many variables involved in economic sanctions from one country and apply them to an analysis of future success or failure with another country.

Economic sanctions are used against target countries in three main ways: limiting exports of the target country, restricting imports from the target country, and impeding the flow of finance to the target country.<sup>35</sup> In essence, for a successful sanctions regime to work, the “costs of defiance borne by the target must be greater than its perceived costs of compliance.”<sup>36</sup> Sanctions are always undertaken by the sender nation(s) with some foreign policy goal in mind. These have varied in objective, duration, and scale, since economic sanctions were first used in the modern international arena, by President Wilson in the First World War to boycott German goods.<sup>37</sup>

Foreign policy goals associated with sanctions are diverse and their use as a tool for foreign policy remains controversial. The most common foreign policy goals in the last century that have been associated with economic sanctions include: changing a target-country’s internal policies (human rights, support to terrorism); changing a target country’s foreign policies (cessation of territory, redrawing a border); change a target country’s regime (destabilize governments, democratize); disrupting a target country’s military potential (development of weapons of mass destruction); and disrupting a target country’s military adventure (assisting a revolution, destabilizing an occupation).<sup>38</sup> Although unspoken by political leaders, economic sanctions often are used to satisfy other foreign and domestic objectives to “do something.” The use of economic sanctions against a target can be enormously satisfying to a domestic and international audience, even if the mechanics are ultimately ineffective against the target country itself. “The mere act of initiating sanctions justifies the rhetorical campaign against a foreign power, provides a rallying cry for stronger measures, and gives domestic lobbies some leverage over the foreign regime.”<sup>39</sup>

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<sup>35</sup> Hufbauer, *Economic Sanctions Reconsidered*, 44–45.

<sup>36</sup> *Ibid.*, 50.

<sup>37</sup> *Ibid.*, 1.

<sup>38</sup> *Ibid.*, 52–53.

<sup>39</sup> *Ibid.*, 54.

How then are economic sanctions' impacts best assessed and better tailored to meet these political goals? Most sanctions regimes tend to focus on these external variables in relation to some political goal and do not take into account the true effects on the actors and their intra-relationships within the target state. This actor-centric approach is critical to focusing sanctions to achieve the political effects desired. This approach takes economic sanctions analysis down another level, and can lead to a more productive approach.

A brief understanding of the Iranian political economy is necessary before continuing further. The state has grown to control 80 percent of the economy, which subjugates the enfeebled private sector, making it dependent upon the public sector.<sup>40</sup> The actors that control this public economy are linked to the highest levels of politics. Since the ascension of Ayatollah Ali Khamenei to the office of supreme leader in 1989, the internal balance of power has changed significantly among actors in Iran.<sup>41</sup> The largest beneficiaries of this change were the conservative elements of the military-industrial complex to specifically include the security services of the IRGC and Basij, whose patronage was cultivated to counterbalance other actors in the system who opposed Khamenei's ascension, based on his weak religious credentials.<sup>42</sup> These security services began branching out into business transactions in the 1990s to spur development and have "accelerated even more during Ahmadinejad's presidency."<sup>43</sup> This expansion was accompanied by the use of an informal network of former IRGC officials and veterans, who often run the subsidiaries, and remains linked to the IRGC via patronage.<sup>44</sup> This phenomenon is not new in Iran, as the clerically controlled bonyads, the largest of which are overseen directly by the supreme leader,<sup>45</sup> control vast wealth, ostensibly for

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<sup>40</sup> D. Zahedi, Prospects for Democratization in Iran: Policy Implications, *Insight Turkey* 12, no. 2 (2010), 223.

<sup>41</sup> Wehrey, *The Rise of the Pasdaran: Assessing the Domestic Roles of Iran's Islamic Revolutionary Guards Corps* [Electronic Resource], National Defense Research Institute (U.S.), 80.

<sup>42</sup> Ibid.

<sup>43</sup> Ibid., 56.

<sup>44</sup> Ibid.

<sup>45</sup> Ibid., 57.

charitable purposes, and have operated in a similar fashion since the Shah's reign.<sup>46</sup> It is through these networks that the state controls so large a percentage of the Iranian economy today, where political actors have both public and private ownership of the opaque economy. Privatization efforts, ostensibly supported by the supreme leader in 2005, to reduce the size of the government's public holdings, have not truly privatized the economy. These efforts have only resulted in these same elite individuals increasing their own private holdings via expanded crony capitalism.<sup>47</sup> Sanctions are having an impact on these actors, raising their costs of imports and production, requiring the government to pay cash subsidies directly to the populace to offset the increase in prices.<sup>48</sup> But these actors are also entrenching further to capitalize from the sanctions, as the IRGC controls "a vast shadow economy of illicit enterprises that are hidden from public view."<sup>49</sup> These enterprises, engaged in black-marketeering, assist in the avoidance of sanctions while making a substantial yearly profit for the IRGC,<sup>50</sup> all the while allowing legitimate sanctions enforcement to undermine their domestic competition and enemies at home.<sup>51</sup>

This literature review of sanctions therefore focuses on the ongoing debate between the differing groups of academics regarding Iranian sanctions, and in doing so, three areas of consensus with the objective of convincing Iran to abandon its nuclear weapons pursuit have been identified: Iranian economic sanctions need to be draconian in their application to achieve their objectives; sanctions need to be supplemented with more diplomacy to achieve their objectives; and economic sanctions need to be abandoned altogether in favor of other alternatives to achieve their objectives.

It is also important to provide a brief background of recent developments with the Iranian nuclear issue before delving into the differing opinions surrounding the use of

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<sup>46</sup> Wehrey, *The Rise of the Pasdaran: Assessing the Domestic Roles of Iran's Islamic Revolutionary Guards Corps* [Electronic Resource], National Defense Research Institute (U.S.), 80.

<sup>47</sup> "Iran Economy: Dial I for IRGC?" *EIU ViewsWire* (9 October 2009).

<sup>48</sup> Jay Solomon and Farnaz Fassihi, "Iran Redistributes Wealth in Bid to Fight Sanctions," *Wall Street Journal (Online)*, sec. Middle East News, 27 July 27, 2011. Doi:27 July 2011.

<sup>49</sup> Wehrey, *The Rise of the Pasdaran* [Electronic Resource]: *Assessing the Domestic Roles of Iran's Islamic Revolutionary Guards Corps*, 64 National Defense Research Institute (U.S.).

<sup>50</sup> *Ibid.*, 64–65.

<sup>51</sup> Alfoneh, "All the Guard's Men: Iran's Silent Revolution," 78.

economic sanctions against Iran. The main concern of the UN is that Iran is engaged in a deception campaign against the International Atomic Energy Agency (IAEA)—an autonomous organization that reports to the UN—designed to enrich enough Uranium Hexafluoride (UF<sub>6</sub>) to the 90 percent High Enriched Uranium (HEU) threshold required to make a nuclear weapon (also known as weapons grade). To achieve this goal, Iran will need to enrich 1200 kilograms of its 3.5 percent (low enriched) Uranium (LEU) to make one nuclear weapon.<sup>52</sup> As of May 2010, Iran is estimated to have twice this amount of 3.5 percent LEU in its stockpile.<sup>53</sup> In February 2010, President Ahmadinejad announced Iran would begin enriching its Uranium stockpile to 20 percent to provide fuel rods for its Tehran Research Reactor,<sup>54</sup> which has legitimate medical uses in cancer treatments.<sup>55</sup> This is alarming because it brings Iran one step closer to the 90 percent weapons grade mark, provided Iran continues enrichment, which would only take a few weeks to complete (from the 20 percent mark), since most of the effort of Uranium enrichment occurs in the beginning stages.<sup>56</sup> Also, Iran does not have the fuel-fabrication capability to turn this 20 percent enriched Uranium into fuel rods for its research reactor and this raises questions as to its true intentions.<sup>57</sup> Iran will need outside assistance to produce these fuel rods and be required to send its enriched Uranium beyond its borders to complete the process, but has consistently delayed in its negotiations to do so. International critics contend that “as long as the [LEU] remains within Iran’s borders, whether under IAEA seal or not, it would be susceptible to seizure and diversion to weapons use.”<sup>58</sup>

Given this alarming situation, one can understand the imperative for the UN to respond. In 1968, Iran signed the Nuclear Non-Proliferation Treaty, which allows it to

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<sup>52</sup> Fitzpatrick, *Iran: The Fragile Promise of the Fuel-Swap Plan*, 68.

<sup>53</sup> *Ibid.*, 72.

<sup>54</sup> Brendan Taylor, *Sanctions as Grand Strategy* (Abingdon, Oxon: Routledge, for the International Institute of Strategic Studies, 2010), 59.

<sup>55</sup> Fitzpatrick, *Iran: The Fragile Promise of the Fuel-Swap Plan*, 68.

<sup>56</sup> Taylor, *Sanctions as Grand Strategy*, 79.

<sup>57</sup> Fitzpatrick, *Iran: The Fragile Promise of the Fuel-Swap Plan*, 78.

<sup>58</sup> *Ibid.*, 74.

develop research concerning the production of nuclear energy for peaceful purposes.<sup>59</sup> Iran argues that its activities are indeed in pursuit of such peaceful policies. However, as a signatory, Iran is also required to give the IAEA prior notification of any Uranium conversion or enrichment activities.<sup>60</sup> Iran failed to report even the existence of its Uranium enrichment facility at Natanz in 2002 and failed to report its initial conversion (a precursor to enrichment) activities beginning on 8 August 2005 at the same location.<sup>61</sup> These failures form the basis of the IAEA noncompliance findings as of September 2005, and the subsequent UN demand, in 2006, that Iran halt its enrichment activities<sup>62</sup> (UNSCR 1696) and follow-on sanctions in 2007<sup>63</sup> (UNSCR 1737 and 1747), 2008<sup>64</sup> (UNSCR 1803) and 2010<sup>65</sup> (UNSCR 1929). These waves of sanctions have “primarily targeted Iranian persons, entities, and banks that [UN] council members determined were involved in Iran’s nuclear and missile programs.”<sup>66</sup> Unilateral U.S. sanctions targeting Iran’s energy sector, as seen in the Iran and Libya Sanctions Act (ILSA) and Comprehensive Iran Sanctions, Accountability, and Divestment Act (CISADA) amendments also seek to alter the regime’s nuclear policy.

Going into the full economic impacts and details of the successive waves of sanctions will be addressed in the main body of thesis research and is outside the scope of this literature review, but comes full circle to the point—will economic sanctions and diplomatic efforts be able to change Iranian political policy with respect to its pursuit of enriched Uranium, presumably to produce a nuclear weapon? If current efforts are not

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<sup>59</sup> Zehra Nilufer Karacasulu and Irem Askar Karakir, “Attitudes of the International Community Toward Iran’s Nuclear Puzzle,” *Journal of International and Area Studies* 15, no. 2 (December 2008), 4.

<sup>60</sup> Taylor, *Sanctions as Grand Strategy*, 63.

<sup>61</sup> *Ibid.*, 63.

<sup>62</sup> J. Crook, “Continuing U.S. Efforts to Discourage Iran’s Nuclear Program,” *The American Journal of International Law* 101, no. 3 (July 2007), 666.

<sup>63</sup> *Ibid.*, 667.

<sup>64</sup> Taylor, *Sanctions as Grand Strategy*, 66.

<sup>65</sup> Katzman, *Iran Sanctions*, 6.

<sup>66</sup> Peter Crail, “West may Seek Alternative Sanctions on Iran,” *Arms Control Today* 38, no. 9 (November 2008), 55.

working, what will? What effects will these sanctions have on the regime leadership, and what will their reactions be? And what new sanctions can be adopted to achieve political effects?

### **3. Expanded Sanctions Can Have Political Effects**

The first academic consensus group argues that existing economic sanctions should be used to their fullest extent and that additional aggressive (i.e., draconian) economic sanctions should be imposed on Iran as soon as possible to change their nuclear policy. This group argues that Iran is currently extremely vulnerable to the present economic downturn and subsequent decrease in worldwide energy prices, as well as to the additional pressure brought on other segments of their economy (external financing and suppliers, insurance, and imports), and would bring Tehran back to the negotiating table.<sup>67</sup> They also argue that Iran is politically vulnerable following its general post-2009 election unrest.<sup>68</sup> They contend that the U.S. is still in a commanding position in the global economy and that even expanded unilateral sanctions would have a global effect since 1) New York is still the global financial center, 2) the dollar remains the clearing currency for petroleum, and 3) regulatory steps taken by the U.S. are mirrored in international markets.<sup>69</sup> Obviously, such steps would raise concerns for an international consensus to all these sweeping sanctions, but this group feels that Iran's trading partners would clearly choose the U.S. over Iran if given an ultimatum.<sup>70</sup> This group has identified several steps to be taken as a way ahead: The UN sanctions track should be pursued more aggressively and even expanded; the UN should better enforce existing sanctions on its books (i.e., establish an independent UN team to monitor Iranian compliance to sanctions); and the U.S. should independently utilize its full sanctions

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<sup>67</sup> Juan Zarate, "Harnessing the Financial Furies: Smart Financial Power and National Security," *The Washington Quarterly* 32, no. 4 (October 2009), 58.

<sup>68</sup> Maloney, "Sanctioning Iran: If Only it were so Simple," 138.

<sup>69</sup> Zarate, "Harnessing the Financial Furies," 58.

<sup>70</sup> Ilan Berman, "Toward an Economic Strategy Against Iran," *Comparative Strategy* 27, no. 1 (January 2008), 22, doi:10.1080/01495930701839621.



powers as authorized by recent congressional legislation.<sup>71</sup> One aspect of Iran's economy identified as being particularly vulnerable is its imports of refined petroleum, of which 40 percent is imported from abroad.<sup>72</sup> U.S. congressional legislation has recently been passed allowing for the sanctioning of actors in this sector of the economy.<sup>73</sup> In summary, this group argues that "an approach that incorporates aggressive financial pressure remains the most likely path to success,"<sup>74</sup> with success presumably being defined as Iran being brought to its knees, financially, and forced to change its behavior with respect to its nuclear enrichment program.

#### **4. Sanctions Can Have Political Effects If Used with Diplomacy**

An alternative academic argument to forcing Iran to alter its behavior through punitive economic sanctions is to coerce it to do so via existing sanctions and expanded diplomacy (i.e., an aggressive "carrot and stick" approach). This group argues that it is a common mistake to look for sanctions to achieve results on their own, especially if not followed up with appropriate reinforcement for negotiation at the bargaining table.<sup>75</sup> Specifically, economic sanctions can complement diplomacy when they give a country an incentive to bargain.<sup>76</sup> Sanctions should also be specifically tailored to achieve goals, and should be balanced to achieve multi-national support and sustainability.<sup>77</sup> Economic sanctions also need to be flexible and adjusted quickly when objectives are not met (expanded), or when they are met successfully (reduced or removed).<sup>78</sup> This group argues that existing U.S. sanctions and rhetoric "create the perception that U.S. sanctions are

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<sup>71</sup> Michael Jacobsen, "Sanctions Against Iran: A Promising Struggle," *The Washington Quarterly* 31, no. 3 (Summer 2008), 81.

<sup>72</sup> Berman, *Toward an Economic Strategy Against Iran*, 20.

<sup>73</sup> Meghan L. Sullivan, "Iran and the Great Sanctions Debate," *The Washington Quarterly* 33, no. 4 (October 2010), 14, doi:10.1080/0163660X.2010.516638.

<sup>74</sup> Jacobsen, *Sanctions Against Iran*, 84.

<sup>75</sup> Sullivan, *Iran and the Great Sanctions Debate*, 12.

<sup>76</sup> J. Walsh, T. Pickering and W. Luers, "Iran and the Problem of Tactical Myopia," *Arms Control Today* 39, no. 10 (December 2009), 15.

<sup>77</sup> Sullivan, *Iran and the Great Sanctions Debate*, 13.

<sup>78</sup> *Ibid.*, 18.

focused on regime change [rather] than restarting negotiations.”<sup>79</sup> Therefore, current sanctions strategies against Iran are flawed from the outset as they lack a coherent strategic goal, which is to coerce Tehran to negotiate away its pursuit of enriched Uranium in exchange for other concessions. This group also argues that the existing set of complex sanctions also lack the capability to quickly reward or punish additional steps taken by Iran on this issue.<sup>80</sup> Finally, this group argues that the current International support for further sanctions against Iran (and third parties) will likely not last and that only carefully crafted sanctions with these carrot and stick approaches will be agreed to in the future.<sup>81</sup>

## **5. Sanctions Should Be Abandoned and Will Not Have Political Effects**

The final group of consensus argues that sanctions ‘will not work against Iran at all and should be abandoned as the Iranian regime will not alter its pursuit of enriched Uranium based on a financial threat. Their first point is that economic sanctions against Iran are legally controversial in that it cannot be proven that Iran’s Uranium enrichment, is not, in fact, for peaceful purposes.<sup>82</sup> Secondly, economic sanctions, as they currently exist, are weak, and while they have hurt the economy, they will not provide a deterrent to Iranian behavior.<sup>83</sup> Thirdly, economic sanctions against Iran are not sustainable in that most countries simply will not embrace them, and will continue to trade with Iran—especially in the oil and gas sector.<sup>84</sup> They also argue that the use of economic sanctions against Iran also presents a double-standard, in that Israel (who never signed the nuclear nonproliferation treaty) has nuclear weapons and there are no economic sanctions against

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<sup>79</sup> Sullivan, *Iran and the Great Sanctions Debate*, 16.

<sup>80</sup> *Ibid.*, 9.

<sup>81</sup> *Ibid.*, 14.

<sup>82</sup> Dingli Shen, “Can Sanctions Stop Proliferation?” *The Washington Quarterly* 31, no. 3 (Summer 2008), 93.

<sup>83</sup> Andrew Parasiliti, “Iran: Diplomacy and Deterrence,” *Survival* 51, no. 5 (October-November 2009), 8, doi:10.1080/00396330903309824.

<sup>84</sup> Shen, *Can Sanctions Stop Proliferation?*, 93.

them.<sup>85</sup> Why is the world not concerned about Israel when Iran has already agreed by treaty to only use enriched uranium for peaceful purposes? They also argue that further sanctions, specifically targeted against Iran's petroleum sector will backfire—as Iran has beefed up its refining petroleum reserves and implemented a quota and rationing program designed to limit domestic consumption.<sup>86</sup> This has resulted in Iran reducing its dependence on foreign-supplied refined petroleum from 40 percent to 20 percent.<sup>87</sup> Neighboring countries, seeing an opportunity for profit, would also assist Iran to “bust the sanctions”<sup>88</sup> and Russia and China will almost certainly water down further proposed sanctions, as they have with the first three rounds of UN sanctions, and the ultimate strategic objective will continue to elude the UN.<sup>89</sup> Given this set of arguments against sanctions, this group has also identified several steps to pursue as a way ahead: first, back-channel negotiations should be employed in future negotiations so Iran does not appear to be publicly pressured;<sup>90</sup> second, a new diplomatic forum needs to be used instead of European Union (EU) negotiations (such as a UN-sponsored Gulf Security Conference) where regional states are brought into the discussion;<sup>91</sup> third, the U.S. should employ a high-level envoy to kick-start the process;<sup>92</sup> fourth, the U.S. should improve on the Palestinian situation and take the initiative away from Iran on regional issues;<sup>93</sup> and fifth, the U.S. should continue to take the moral high ground with respect to Iran, and make public speeches on positive developments on the Iranian enrichment situation, versus making threats against Iran.<sup>94</sup> Actual engagement with Iran should focus on

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<sup>85</sup> D. Robicheau, “Sanctions on Iran: What’s Missing from Obama’s New Dialogue,” *Monthly Review* 61, no. 10 (March 2010), 5.

<sup>86</sup> Willem Kemenade, “China Vs. the Western Campaign for Iran Sanctions,” *The Washington Quarterly* 33, no. 3 (August 2010), 109, doi:10.1080/0163660X.2010.492344.

<sup>87</sup> *Ibid.*, 109.

<sup>88</sup> *Ibid.*

<sup>89</sup> *Ibid.*, 108.

<sup>90</sup> Parasiliti, *Iran: Diplomacy and Deterrence*, 10.

<sup>91</sup> *Ibid.*, 11.

<sup>92</sup> *Ibid.*

<sup>93</sup> *Ibid.*

<sup>94</sup> Parasiliti, *Iran: Diplomacy and Deterrence*, 10.

security guarantees, economic benefits and support for the right of peaceful nuclear technology and ways to assist in achieving this end.<sup>95</sup>

## **6. Literature Review Conclusion**

This review highlights a few key points with respect to the Iranian nuclear issue. First, there is no common academic consensus on how to proceed, although the Obama administration appears to be favoring the sanctions and diplomacy approach.<sup>96</sup> Secondly, all parties agree that the Iranian leadership (and their negotiators) have consistently stated that they will not negotiate away their enrichment rights, no matter what is offered or threatened against them. This would indicate that the independent variable (sanctions) will have absolutely no effect on the dependent variable (change in behavior). One would then consider alternative independent variables to achieve this effect. Surprisingly, one thing all parties agree on is that a military strike against Iran (by any nation) to eliminate its nuclear facilities is the absolute worst possible option, given Iran's ability to project power in the Persian Gulf region, disrupt shipping lanes, and unleash potential terrorist attacks across the world. "In the aftermath of an unprovoked attack, Iran could be expected to withdraw from the NPT and engage the full resources of a unified nation in a determined nuclear-weapons-development programme."<sup>97</sup> The most incomplete area of research found with this literature is that there are no existing estimates or data as to exactly what level of financial "pain" the Iranian leadership is willing to tolerate before it changes its policies. Applications of sanctions are only effective if they achieve a political goal. Other gaps include the level of population tolerance to prolonged (severe) economic sanctions, costs to countries imposing sanctions (both economic and political), and other potential areas of political vulnerability the regime faces dealing with prolonged economic hardship. More research into this subject would have profound U.S. policy implications.

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<sup>95</sup> Arsalan Ghorbani Sheikhneshin, "Iran and the US: Current Situation and Future Prospects," *Journal of International and Area Studies* 16, no. 1 (June 2009), 111.

<sup>96</sup> Sullivan, *Iran and the Great Sanctions Debate*, 11

<sup>97</sup> Fitzpatrick *The Iranian Nuclear Crisis: Avoiding Worst-Case Outcomes*, International Institute for Strategic Studies, 8.

## E. METHODS AND SOURCES

The analytical approach that will be taken in the research and production of this thesis will include a historical study of past sanctions cases, specifically the Iraqi and South African sanctions regimes as unitary actor and democratic states, respectively. Iranian sanctions will also be reviewed, and the current effects on their factionalized political economy will be examined. Research will draw conclusions as to the efficacy of these current and historical economic sanctions regimes on altering Iranian policy and recommending alternative or additional sanctions regimes (including accompanying diplomatic policies) to achieve intended political results. A closer examination of the Iranian political actors and their client constituencies will also be presented, to understand the actors' behaviors, determine their interests, and identify their vulnerabilities. Finally, the efficacy of Iranian sanctions will be assessed and new recommendations will be presented to achieve a change in the Iranian political economy. This will include an analysis of new sanctions' potential chances of success given the political and economic constraints they will face. As stated previously, the official policy of the UN remains to deny Iran the legitimacy of its enrichment programs (i.e., zero-tolerance for enrichment),<sup>98</sup> let alone developing the "physics packages" needed to weaponize such Uranium while continuing development on long-range delivery systems.<sup>99</sup> Sanctions regimes must alter the political economy to an extent to achieve these goals.

Important works that specifically address the Iranian sanctions case include: *Shrewd Sanctions* by Meghan O'Sullivan; and *Feeling Good or Doing Good with Sanctions* by Ernest Preeg. Numerous academic and governmental publications also supplement these primary sources.

Other important research available on the Iranian Political Economy include: *Globalization and the Politics of Development in the Middle East* by Clement Moore

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<sup>98</sup> Fitzpatrick, *The Iranian Nuclear Crisis: Avoiding Worst-Case Outcomes*, International Institute for Strategic Studies, 8.

<sup>99</sup> *Ibid.*, 13.

Henry and Robert Springborg; and *A Political Economy of the Middle East* by Alan Richards and John Waterbury. Numerous academic and governmental publications also supplement these primary sources.

## **F. THESIS OVERVIEW**

This thesis observes the standard convention of five chapter delineations to include: An introductory chapter, three chapters of research and background, and a concluding analytical chapter where new findings are put forth to address the observed gap in knowledge. Chapter II will review historical sanctions cases, including Iraq, South Africa, and Iran to compare unitary, democratic and fragmented political economies. Chapter III will identify the actors and their constituencies in the Iranian political economy, as well as their behaviors, interests and vulnerabilities. Chapter IV will review the past and current sanctions regimes targeted at Iran, and assess their effects on the political economy, and recommend alternative economic sanctions regimes and diplomatic activities to achieve the political effects desired. Finally, Chapter V will present the recommended sanctions course of action given this actor-centric approach to best achieve the political goals desired.

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## II. REASSESSING SANCTIONS REGIMES

Economic sanctions are defined as “deliberate, government inspired withdrawal, or threat of withdrawal, of customary trade or financial relations.”<sup>100</sup> Policymakers in the U.S. (and diplomats in the UN) are quick to impose economic sanctions upon other states in response to their government’s unfavorable policy decisions. Sanctions are a common coercive means of diplomacy that have become the primary tool of choice when censuring states and their policies. “Sanctions are part and parcel of international diplomacy, a tool for coercing target governments into particular avenues of response.”<sup>101</sup>

In sum, the imposition of sanctions conveys a triple signal: To the target country it says the sender(s) does not condone the target’s actions; to allies it says that words will be supported with deeds; and to domestic audiences it says the sender government will act to safeguard the nation’s vital interests.<sup>102</sup>

A survey of the historical use of sanctions by the United States indicates a number of reasons for their use:

Sanctions have been deployed to pursue a number of foreign policy goals other than those related to warfare and national security... during the Cold War these episodes often found a superpower pitted against a smaller and formerly friendly country gone “astray.”<sup>103</sup>

Following World War I, the idea that economic sanctions could be used as an alternative to armed conflict gained worldwide recognition and popularity, yet “through World War II, the objectives sought with the use of sanctions retained a distinctly martial flavor.”<sup>104</sup> Economic sanctions have become a prominent part of U.S. foreign policy, participating in 118 cases of unilateral and/or joint sanctions cases between 1914 and

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<sup>100</sup> Hufbauer, *Economic Sanctions Reconsidered*, 3.

<sup>101</sup> *Ibid.*, 5.

<sup>102</sup> *Ibid.*, 7.

<sup>103</sup> *Ibid.*, 13.

<sup>104</sup> *Ibid.*, 10.



2007 (out of a total of 187 worldwide cases).<sup>105</sup> Most cases of sanctions after the Cold War have had varying objectives, but regime change (specifically encouraging democratic reforms or the restoration of democracy) has been the main objective in almost half of the cases, with a few successes, but most cases ended in failure.<sup>106</sup> Other objectives of sanctions during this period include efforts to “settle expropriation claims, to counter drug lords, and to combat international terrorism.”<sup>107</sup>

Sanctions have a troubled track record achieving their objectives due to a number of variables. Often, the political objectives of the sanctions are not met, despite the economic success of the sanctions against the target country. Yet, sanctions continue to be used as a form of state censure, as alternatives are viewed as unacceptable. “Military action would be too massive and diplomatic protest too meager.”<sup>108</sup> This chapter will examine these variables, review past sanctions cases, including the Iranian case specific to this work—and propose factors for future success.

In the case of Iran, there is evidence that sanctions are having economic effects towards their intended economic objectives, but are still not achieving their intended political objectives. This chapter will begin to investigate the Iranian case by identifying the framework of all the variables of sanctions and their weaknesses and characterize ways to sharpen “smart sanctions” to achieve their intended political effects.

#### **A. VARIABLES IMPACTING ECONOMIC SANCTIONS SUCCESSES AND FAILURES**

Reviewing the literature, there are five main reasons that economic sanctions have historically failed to alter the policy behavior of states. These reasons will be discussed, and to them will be added a fifth reason that is often inadequately considered by designers of sanctions. Smart sanctions can be made “smarter” by designing and implementing sanctions with these considerations taken into account. Additional

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<sup>105</sup> Ibid., 17, 34–38.

<sup>106</sup> Hufbauer, *Economic Sanctions Reconsidered*, 14.

<sup>107</sup> Ibid.

<sup>108</sup> Ibid., 9.

measures supporting sanctions need to be taken by governments in support of sanctions to ensure smart sanctions are effective (i.e., media coverage showing realities of sanctions, law enforcement activities, and diplomatic initiatives).

These variables were primarily drawn from *Economic Sanctions Reconsidered*, a recent work by Dr. Gary Clyde Hufbauer, who has written extensively on international trade, global investments and finance and economic sanctions issues. A number of other authors frequently cite his works on sanctions, in particular, for their own assessments of sanctions cases. Specific to Iran, and independent of Dr. Hufbauer, other scholars have put forth very similar assessment-variable criteria, to include Dr. Nikolay A. Kozhanov's assessment that Iranian sanctions are failing (primarily) due to variables three (weak sanctions enforcement) and four (unpopularity of sanctions internationally) below.<sup>109</sup> Similarly, Dr. Meghan O'Sullivan's assessment of Iranian sanctions failures cites variables one (inadequate sanctions) and five (structure of the political economy) as the primary variables.<sup>110</sup>

## **1. Sanctions Are Inadequate**

Sanctions themselves are most often simply inadequate to accomplish their intended political goals.<sup>111</sup> "The goals may be too elusive; the means too gentle; or cooperation from other countries, when needed, are too tepid."<sup>112</sup> Meeting foreign policy objectives with smart sanctions is in itself a difficult concept. Economists can identify areas of an economy and design smart sanctions to target those areas and have economic impacts. Weak areas of an economy, where supplies of a number of commodities are deficient, could be severely impacted with economic sanctions or embargoes. Strong areas of the economy can also be identified, where exports of the state's commodities could be limited by sanctions or prevention of further investment to exploit resources or

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<sup>109</sup> Nikolay A. Kozhanov, "U.S. Economic Sanctions Against Iran: Undetermined by External Factors," *Middle East Policy* Fall, no. 3 (24 October 2011), 15 November 2011.

<sup>110</sup> O'Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 91–92.

<sup>111</sup> Hufbauer, *Economic Sanctions Reconsidered*, 7.

<sup>112</sup> *Ibid.*, 8.

commodities. However, this is irrelevant if the regime in power refuses to be deterred by sanctions due to the perceived importance of the policy goal.

## **2. Sanctions May Strengthen the Legitimacy of the Targeted Leadership**

If the sanctioned state's leaders have embarked on a policy that is highly popular across the state's policy, the sanctions are doomed to failure and will not result in the policy change the sanctions are designed to coerce. The costs of sanctions will be gladly borne by the population and can easily be used by the leadership to shore up their own legitimacy against opposition groups. "In particular, economic sanctions may unify the target country both in support of its government and in search of commercial alternatives [to the sanctioned commodities]." <sup>113</sup> This is especially true if the leadership maintains tight control of the dialogue over the policy via control of the media and press.

## **3. Enforcement of Sanctions is Weak**

Multilateral enforcement of sanctions is also of vital importance. If sources of imports and outlets for exports can be found by the sanctioned state, the sanctions imposed can be mitigated, and the sanctions have only symbolic value. They would not achieve their intended economic effects and, therefore, have no political effects beyond serving a domestic and international imperative for some kind of action to be taken. "Sanctions may prompt powerful or wealthy allies of the target country to assume the role of 'black knight,' their support can largely offset whatever deprivation results from sanctions themselves." <sup>114</sup> This kind of sanctions avoidance can take the form of direct trade by nonsanctions participating states, or via the grey area of third country intermediaries—foreign subsidiary companies acting as intermediate shipping agents to move sanctioned commodities in and out of third countries to their ultimate destination—the sanctioned state itself. It is critical that states sending sanctions use accompanying measures in support of sanctions to enforce them, such as extensive international law-enforcement cooperation to curtail smuggling.

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<sup>113</sup> Hufbauer, *Economic Sanctions Reconsidered*, 8.

<sup>114</sup> *Ibid.*

#### 4. Sanctions are Unpopular among Sending States

Political and economic goals may not be shared with all sanctions-imposing states,<sup>115</sup> and the degree of the sanctions costs may not be equitable among all imposing states. This can lead to misunderstandings between imposing states, in the best cases, and to falling-out between them that lead to sanctions mitigation in the worst cases. A states' national interest has always tended to trump its foreign alliances, and this includes agreements on multilateral sanctions. Past examples of the worst cases of sanctions misunderstandings regarding objectives have seen anti-sanction legislation introduced by some of the imposing states that actually mitigates the very sanctions (economically and psychologically) they are supposed to be enforcing.<sup>116</sup> Economic costs of sanctions to domestic businesses are also a serious concern, especially if they are perceived as inequitable by the business community. In the past, business interests have successfully lobbied for exceptions to sanctions laws to prevent a loss of sales, business reputation, and reliability.<sup>117</sup> "After the first flush of patriotic enthusiasm, such complaints can undermine a sanctions initiative."<sup>118</sup> Attempts to ensure multilateral cooperation via unilateral sanctions legislation has also created a severe backlash internationally and more waiver options for sanctions that mitigate the intended economic and political effects of sanctions. Past sanctions against Iran have led to amendments to U.S. sanctions laws to allow for waivers that prevent "a potential clash over extraterritorial application of U.S. law."<sup>119</sup> Economic sanctions should therefore be undertaken by sending governments with supporting efforts. These measures include: showcasing the economic and political goals of the sanctions—and solidifying domestic and international support; using extensive media coverage to show the realities of sanctions in the target country

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<sup>115</sup> Hufbauer, *Economic Sanctions Reconsidered*, 8.

<sup>116</sup> *Ibid.*

<sup>117</sup> *Ibid.*, 9.

<sup>118</sup> *Ibid.*

<sup>119</sup> *Ibid.*

(attempting to avoid humanitarian disasters being blamed on sanctions, versus the target country's own economic choices) and; better diplomatic initiatives to gain international support for sanctions.

## **5. Structure of the Target State's Political Economy**

The structure of the target state's economy is often not given enough attention by policy makers when fashioning sanctions. Intimate knowledge of the number of political elite actors and their degree of control over sectors of the economy is critical to fashioning sanctions that achieve their political objectives. The wealth of the targeted state is included in this assessment, as financial and trade sanctions do have a significant impact on the relative wealth of both resource poor and rich states.

Financial sanctions [in the form of withholding aid to poor countries, or a restriction of international finance to wealthy states] offer the potential for greater effectiveness as a foreign policy tool because they are easier to enforce, harder to evade, and may spur market-reinforcing effects.<sup>120</sup>

However, even the most draconian of these types of sanctions have failed to achieve their political objectives. Most states targeted with these types of sanctions have a unitary political elite faction (i.e., a dictatorship autocracy that emasculates or eliminates all political opposition) and is able to withstand the economic effects of these types of sanctions, suppress the internal dissent resulting from them, and thus elude the political goals—even if imposed for a long period of duration.

These types of sanctions have historically been broad in their application and mostly target the economy as a whole, or assets and resources of the political elite. "Asset freezes are also becoming more popular as a means of targeting the leaders of 'rouge' regimes, corrupt autocrats, and their associates."<sup>121</sup> It is hoped that these types of sanctions will coerce the leadership into the desired policy change. Often, the leadership is able to deflect the actual costs of sanctions away from its own assets and resources towards its political competitors or other sectors of the economy. Economic and political

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<sup>120</sup> Hufbauer, *Economic Sanctions Reconsidered*, 47.

<sup>121</sup> Ibid., 63.

factors of the targeted state can be a factor in the ability of the leadership to mitigate these sanctions.<sup>122</sup> If the state is, initially, economically healthy, with normal ranges of inflation and unemployment—and the leadership remains in firm control of the state—then these costs are easier to absorb. Political dissent will be easier to suppress by the leadership, and the policy objectives of the sanctions will be more difficult to achieve. If the state is, initially, economically unhealthy, exhibiting a multitude of economic problems, and the leadership's hold on power and government is questionable, it may be more willing to negotiate to end the sanctions, with the resulting achievement of the political objectives. If the state has abundant resources for export, and the political elite can maintain control of those resources, then dislodging or altering their policies will prove more difficult to do without a very tight sanctions regime that prevents smuggling. If there are legitimate political challengers to power in the state (i.e., a fractured elite), a sanctions regime will more easily achieve its political results.

In cases of democracies, or an autocracy with fragmented elite actors such as Iran, this type of reasoning should find more applicability as at least a nucleus of legitimate political dissent exists within the leadership.

A related finding [in examining sanctions cases] is that sanctions seeking a modest change in policy are more successful against target countries that are relatively more democratic ... democracies are by definition more open to voices advocating a policy shift than autocratic countries. If important internal groups see merit in a policy change, that view is more likely to find advocates within the top circles of a democratic government.<sup>123</sup>

Therefore, the costs of sanctions targeted against legitimate democracies would not be long tolerated as the political economy is diffused among many actors with a voice in government. "Past experience suggests that punitive sanctions are most likely to be effective in societies where there is some degree of democracy and social openness."<sup>124</sup>

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<sup>122</sup> Hufbauer, *Economic Sanctions Reconsidered*, 62.

<sup>123</sup> *Ibid.*, 67.

<sup>124</sup> Euclid A. Rose, "From a Punitive to a Bargaining Model of Sanctions: Lessons from Iraq," *International Studies Quarterly* 49, no. 3 (September 2005), 470.

In an autocracy with a fragmented elite, this concept is still sound, but sanctions are often misapplied as if a unitary elite were in complete political and economic control of the state. Sanctions designed to weaken the assets and resources of the biggest political actor (usually the actor most resistant to the desired policy change) are designed and implemented, and while their economic effects can be argued on a case-by-case basis, usually result in failure. The largest political actor usually has the most control of the political economy and can shift the costs of sanctions to other actors (and sectors of the economy under their control) while preserving their own assets and resources. Similar sanctions that limit foreign direct investment (FDI), foreign aid, and punishment of human rights abuses are targeted too broadly and are usually ineffective against a political economy with a fragmented elite.

## **B. BRIEF ECONOMIC CASE STUDIES**

In order to lay a framework for these variables, a brief review of several cases of economic sanctions against targeted states is necessary. These cases will examine the sources of failure and determine their impacts and reasons for failure in achieving their political objectives. Cases reviewed will include a unitary autocracy (Iraq), a democracy (South Africa), and a fragmented autocracy (Iran).

### **1. Sanctioning Iraq**

Iraq under Saddam Hussein can easily be characterized as one of the most brutal dictatorship autocracies in history. Brooking no dissent, political oppositionist actors to the Baathist regime were ruthlessly eliminated. Potential political opposition was co-opted and coerced to become the regime's closest supporters. This was done with patronage, outlays of capital and rents dispensed from the regime to these actors, while simultaneously (and ultimately) threatening them with elimination should any hint of threat or independent power base manifest itself behind any of these actors.<sup>125</sup> The power of this "sword" and the ability to eliminate rivals became the ultimate guarantor of

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<sup>125</sup> Clement M. Henry, Robert Springborg, *Globalization and the Politics of Development in the Middle East*, 2nd ed. (New York: Cambridge University Press, 2010), 158.

Saddam's structural power in Iraq.<sup>126</sup> As a unitary actor firmly in control of the political economy, Saddam Hussein's regime and the co-opted network of family, military/security apparatuses and connected tribal leaders—all acting in unison—weathered years of economic sanctions, which were devastating, economically, to the Iraqi state and failed in all their political objectives.

Detailing the waves of economic sanctions and their micro-level economic effects is beyond the scope of this work. But a broad examination of sanctions relative to the historic reasons for failure is necessary, and this examination will reveal that, ultimately, a unitary actor firmly in control of the political economy can more easily influence the other variables to frustrate the political goals sanctions are designed to achieve. Economic sanctions against Iraq from 1990–2003 fall in two broad periods: the first from 1990–1996; the second from 1997–2003.<sup>127</sup> These periods will be briefly examined for the variables most responsible for their failure.

*a. Iraqi Sanctions 1990–1996*

Iraq's economy was already severely weakened prior to the onset of sanctions in August 1990 due to the Iran–Iraq war. Iraq was heavily in debt to its Arab neighbors and its economy severely damaged from the war.<sup>128</sup> Policymakers assumed that sanctions would, therefore, quickly bite and Saddam would fold to UN demands. “They anticipated that Iraq would grudgingly, but quickly, comply with UN resolutions, paving the way for the lifting of sanctions and the resumption of more normal, if guarded, relations with the international community. None of these expectations materialized.”<sup>129</sup> Further damage from the six-week Desert Storm campaign, designed to disrupt the Iraqi military's command, as well as its logistical, petroleum, and industrial capabilities, further damaged the entire economy.<sup>130</sup>

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<sup>126</sup> Ibid., 157.

<sup>127</sup> O'Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 128.

<sup>128</sup> Ibid., 123.

<sup>129</sup> Ibid., 105.

<sup>130</sup> Ibid., 123.



Economic sanctions imposed during this period therefore, had a head start and did achieve their economic objectives, and came close to achieving their political ones by 1996. “The multilateral, comprehensive sanctions regime put in place terminated virtually all legal, nonhumanitarian trade—both military and civilian—between Iraq and the rest of the world.” Virtually isolated from the outside world during this period, Saddam’s regime did what it could to maintain its patronage networks, while keeping the population at the subsistence level. “Efforts to maintain food supplies and to accumulate foreign exchange from any source were crucial to Saddam’s efforts to protect his inner circle [during this time].”<sup>131</sup> These financial and trade sanctions were devastating economically, and in choosing its own survival over the welfare of his people, Iraq’s humanitarian crisis worsened.

By the middle of the 1990s, sanctions and Saddam’s mismanagement of the economy had caused a major economic crisis.<sup>132</sup> Hyper-inflation, the growth of a sizable shadow economy (to include smuggling oil) and especially the inability to pay for food imports had forced Saddam to implement austerity measures and begin negotiations for the Oil for Food Program, finalized in November 1996.<sup>133</sup> Without this agreement (acceptance of UN Resolution 986, the oil for food program), Saddam’s ability to stabilize the economy—his ability to maintain his patronage networks while keeping the population at subsistence level—would have evaporated and his regime would have faced “economic collapse and political turmoil.”<sup>134</sup> This eventuality was not an objective of the sanctions during this period and humanitarian concerns outweighed the economic effects on the regime. Sanctions had almost achieved their political goals.

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<sup>131</sup> O’Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 129.

<sup>132</sup> *Ibid.*, 130.

<sup>133</sup> *Ibid.*

<sup>134</sup> *Ibid.*, 115.

**b.      *Iraqi Sanctions 1997–2003***

“Until the Oil for Food program got underway in 1997, hardly any goods crossed Iraq’s borders in either direction.”<sup>135</sup> Economic sanctions had severely weakened the Iraqi economy, but the start of the oil for food program untied one of Saddam’s hands. Previously contending with food rationing and paying for food with limited foreign receipts to keep the population at subsistence level, this program freed him to instead focus on maintaining and expanding his patronage networks to his potential rivals and key supporters, especially his armed forces.<sup>136</sup> His ability to fully rebuild his armed forces, however, remained limited to funding from illicit activities.<sup>137</sup>

Sanctions continued to incur huge costs on the Iraqi economy despite the oil for food program, but Saddam used this to his advantage, blaming economic problems both internationally and domestically on the sanctions versus his own economic priority choices. “In the absence of sanctions, Iraq could have expected to export more than \$250 billion in oil and other goods from 1990 to 2000—approximately \$200 billion more than it actually did even when the exports under the Oil for Food program are taken into account.”<sup>138</sup> Saddam, instead, co-opted oil smuggling networks and expanded them to bring in extra cash to his regime, as this proved to be extremely profitable and kept his regime in place.<sup>139</sup>

Sanctions on oil—the key to achieving the political goals—were busted directly through the oil for food program as well, as Iraq was able to increase its oil production capabilities, and regional neighbors assisted with the smuggling abroad.<sup>140</sup> “Illicit sales rose as oil production increased and the legal export of oil under the Oil for Food Program made smuggling more difficult to detect.”<sup>141</sup> Iraq also sought petroleum

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<sup>135</sup> Ibid., 125.

<sup>136</sup> O’Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 132.

<sup>137</sup> Ibid., 125.

<sup>138</sup> Ibid.

<sup>139</sup> Ibid., 132.

<sup>140</sup> Ibid.

<sup>141</sup> Ibid.

development project contracts (under the oil for food program) specifically with states influential at the UN who had a vested interest in ending the sanctions,<sup>142</sup> and with “foreign companies seeking to market Iraqi oil,”<sup>143</sup> many of whom were:

Unknown ... many of them apparently based in countries more sympathetic to Iraq. Less subject to international scrutiny than major oil companies, these firms allowed Iraq to continue exporting oil through favored middlemen with less oversight from the UN or western governments.<sup>144</sup>

The worsening humanitarian situation during this period, of which sanctions were perceived as being the only culprit, was also influencing worldwide public opinion toward sanctions. Multiple studies and reports blamed the worsening humanitarian situation in Iraq squarely on the “punitive” economic sanctions in place,<sup>145</sup> versus the economic choices of a brutal dictatorship intent on staying in power at any price. These studies blamed sanctions as being solely responsible for the plunging of Iraq’s per capita income and the caloric intake of its citizens to the lowest in the world (i.e., Bangladesh, Haiti, and Ethiopia), increasing diseases and premature child deaths and destroying the societal safety net of the country.<sup>146</sup> The perception that sanctions alone caused the worsening humanitarian situation prompted even successive UN secretary generals to question the legitimacy of economic sanctions at all.<sup>147</sup>

### *c. Iraqi Sanctions Assessment*

Adequacy of Sanctions: Sanctions during this time were adequate for accomplishing their economic objectives, but inadequate for the political objectives set (i.e., modifying regime behavior), primarily because the structure of the Iraqi political economy was controlled by a unitary elite. Sanctions were not left in place long enough

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<sup>142</sup> Ibid., 133.

<sup>143</sup> Ibid.

<sup>144</sup> O’Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 135.

<sup>145</sup> Rose, *From a Punitive to a Bargaining Model of Sanctions: Lessons from Iraq*, 467.

<sup>146</sup> Ibid., 467.

<sup>147</sup> Ibid., 468.

to weaken Saddam enough to contend with a rival to power (one who would cooperate with UN demands), and Saddam was given an out based on humanitarian concerns via the oil-for-food program (in which Saddam played a part in spreading the propaganda that sanctions were solely responsible for).<sup>148</sup> Also, the sanctions structure provided Saddam with no incentives to comply with the political demands.<sup>149</sup> The outlet provided by the oil for food program gave Saddam a way to maintain his hold on the political economy due to his unitary hold on economic activity and the allocation of resources to favored actors. Sanctions did have some success weakening the regime. Income from oil exports was virtually nonexistent from 1991–1996,<sup>150</sup> and Iraqi aggression was certainly contained. Important resources were kept out of the hands of the regime, especially military equipment, both conventional and unconventional.<sup>151</sup> However, with the increase of smuggling enabled by willing regional state and nonstate actors and abuse of the oil for food program, Saddam was able to maintain his patronage networks, “providing the elite with access to luxuries and commodity items.”<sup>152</sup>

Strengthening of Legitimacy: Sanctions, in the long run, did not strengthen the legitimacy of Saddam’s rule—but this is irrelevant due to his control of the political economy and security apparatuses. It can be argued that sanctions strengthened the legitimacy of Saddam’s regime and his policies, at least in the first few years.

Saddam did find a number of ways to turn sanctions to his domestic advantage in the short term. Sanctions created an external enemy in the form of the U.S. (more so than the UN) and perpetuated a “siege mentality” in Iraq, both of which the regime exploited to deflect criticism from its rule and to justify its own repressive behavior.<sup>153</sup>

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<sup>148</sup> O’Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 157.

<sup>149</sup> O’Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 159.

<sup>150</sup> Ibid., 131.

<sup>151</sup> Ibid., 140.

<sup>152</sup> Ibid., 137.

<sup>153</sup> Ibid.

Sanctions allowed Saddam to appear to be the people's benefactor via the distribution of free food rations (with the exception of the Kurdistan region).<sup>154</sup> But domestic legitimacy was severely eroded in the long term as sanctions continued to bite, causing serious economic difficulties to the population, while simultaneously weakening the strength of the regime.<sup>155</sup> "More than a decade of sanctions narrowed his base of support considerably, as multiple coup attempts and tribal rebellions over the period suggest."<sup>156</sup>

Enforcement of Sanctions: Iraqi sanctions were not universally enforced, primarily due to regional sanctions fatigue, Saddam's ability to "advance his political agenda through the economic links made possible through the Oil for Food Program,"<sup>157</sup> and the extremely lucrative smuggling activity, which Saddam's regime enabled and depended upon, itself.

Popularity of Sanctions: The popularity of Iraqi sanctions was certainly weak, for several reasons, some for which the United States deserves a measure of responsibility. The breakdown of the Oslo Peace Process in the late 1990s made continuing enforcement of Iraqi sanctions untenable by regional Arab states.<sup>158</sup> Also, Saddam's propaganda did a far better job of shaping debate and international public opinion on sanctions to his favor than the United States did. "The United States made only feeble efforts to counter Saddam's well-orchestrated propaganda campaign to convince the world that sanctions—not his own indifference—were responsible for the suffering of Iraqis."<sup>159</sup> This is also due to the fact that there was no political opposition in Iraq to provide an alternative view. "Perhaps nothing could have shored up international support for sanctions better than a more effective, continuous, and concerted effort...[to

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<sup>154</sup> Ibid.

<sup>155</sup> O'Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 137.

<sup>156</sup> Ibid.

<sup>157</sup> Ibid., 156.

<sup>158</sup> Ibid., 150.

<sup>159</sup> Ibid., 157.

showcase Saddam's] actions to frustrate international humanitarian relief efforts and his preference for spending Iraqi resources on nefarious rather than charitable purposes."<sup>160</sup>

Structure of the Political Economy: Ultimately, the lack of political opposition (due to Saddam's ruthless suppression of it), as well as his unchallenged control of the economy shaped all the other factors relative to assessing Iraqi sanctions. Iraq was an impossible nut to crack with sanctions alone due to the structural power of the regime, based on its complete control of resources, patronage networks, security services, and information. Sanctions were not coupled with incentives to comply, nor were they coupled with further punishment for noncompliance. Instead, little action was taken against Iraq's failures to comply with political demands due to the fractured nature of the international community over sanctions, which can be attributed to Saddam's ability to divide it, politically, with his ultimate control of the Iraqi political economy.<sup>161</sup> "Sanctions were less effective against the dictatorial regime in Iraq because domestic opposition groups were unable to exert pressure for political change."<sup>162</sup>

## **2. Sanctioning South Africa**

South Africa is a unique sanctions case, due to its democratic history. But this history is skewed due to the structure of its political economy—one where only a small racial white minority had all voice in an otherwise open parliament. Non-whites could not vote, had no representation based on the constitution, and were sequestered to their own areas of land—and only allowed passage on white lands to work.<sup>163</sup> This white racial minority comprised approximately 15 percent of the population by 1980, but "earned two-thirds of the income and controlled over 80 percent of the land."<sup>164</sup> The unrepresented majorities fought for participation in that government and integration into the broader political system. Prior to the lifting of sanctions in April 1994, the state's

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<sup>160</sup> Ibid.

<sup>161</sup> O'Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 159.

<sup>162</sup> Rose, *From a Punitive to a Bargaining Model of Sanctions: Lessons from Iraq*, 470.

<sup>163</sup> Neta Crawford, Audie Klotz, *How Sanctions Work: Lessons from South Africa* (New York: St. Martin's Press, 1999), 7.

<sup>164</sup> Ibid., 7.

white racial minority found itself under siege from the international community to both end its apartheid policy and to end South African regional aggression—particularly in Namibia, which was under South African occupation—which were the primary goals of the economic sanctions.<sup>165</sup>

Some have argued that sanctions alone did not and could not have brought about the change in the political economy of South Africa, which allowed for the ending of apartheid. This is primarily because South African sanctions in the 1980s were porous, and could be fairly easily avoided by paying a premium. “The direct impact of trade sanctions was limited. South Africa developed extensive measures to circumvent the sanctions, although these sometimes involved costly import-substitution.”<sup>166</sup> The ongoing industrialization of South Africa, and the need for a larger volume of unskilled labor that came from nonwhite minorities, was also certainly a factor for this demographic to demand representation in the democracy.<sup>167</sup> Changing demographics also contributed as the white population was shrinking relative to the nonwhite population, and apartheid could not continue forever.<sup>168</sup> As time went on, reformist politicians also came to power in South Africa, arguably as a result of the perceptions of international sanctions and their changing normative views on apartheid.

#### *a. South African Sanctions*

Forms of South African sanctions had been ongoing since the 1960s, to include an arms embargo during that period, as well as an oil embargo in 1973 by the Organization of Oil Exporting Countries (OPEC). Iran ignored this embargo, becoming South Africa’s primary oil provider until 1979, undercutting the costs of sanctions.<sup>169</sup> Riots and protests against apartheid policies, as well as military incursions into Angola in

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<sup>165</sup> Ibid., 10.

<sup>166</sup> Philip Levy, “Sanctions on South Africa: What did they do?” *The American Economic Review* 89, no. 2 (1999), 417–418. <http://search.proquest.com/docview/233036204?accountid=12702>.

<sup>167</sup> Crawford and Klotz, *How Sanctions Work: Lessons from South Africa*, 13.

<sup>168</sup> Ibid., 14.

<sup>169</sup> Gary Clyde Hufbauer et al., *Economic Sanctions Reconsidered*, 2nd ed. (Washington, DC: Institute for International Economics, 1990), 236.

the late 1970s undermined the perception of political stability in South Africa, resulting in restrictions on private sector loans from concerned multinationals, as well as some governments formally banning direct investment, as well as advocating disinvestment during this time.<sup>170</sup> South Africa weathered some of this storm by borrowing from the International Monetary Fund and by relying on commodities exports (especially a rising price in gold) to maintain its balance of payments.<sup>171</sup> However, by the early 1980s, before the multilateral economic sanctions were put in place, the damage to South Africa's reputation had been done and many private lenders began pulling out based on fears of "political instability and a deteriorating economic situation"<sup>172</sup> touching off a liquidity crisis.

It is important to note South Africa's foreign loan requirements at this time, which it needed for its policy of Import Substitution Industrialization (ISI). South Africa's industrialization, which it viewed as a necessary step in economic development, was changing its political economy and making its policy of apartheid increasingly untenable. Not only did this policy make South Africa more vulnerable to international sanctions to meet its borrowing and trade finance requirements, it was the primary means that the nonwhite majority became politicized.<sup>173</sup> The policies of segregated racial labor laws and living locations advocated by apartheid were increasingly impossible to manage as the country industrialized, and the new nonwhite proletariat class sought increasing political representation in the closed democracy. This factor, combined with a decreasing relative percentage of the white population and the labor/wealth distortions across the economy led to the development of an "effective political movement against the apartheid government,"<sup>174</sup> ultimately leading to the achievement of the political goals of the sanctions regime.

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<sup>170</sup> Crawford and Klotz, *How Sanctions Work: Lessons from South Africa*, 163.

<sup>171</sup> *Ibid.*, 162.

<sup>172</sup> Levy, *Sanctions on South Africa: What did they do?* 417.

<sup>173</sup> Crawford and Klotz, *How Sanctions Work: Lessons from South Africa*, 13.

<sup>174</sup> Levy, *Sanctions on South Africa: What did they do?* 419.



By the time sanctions were put in place, starting in September 1985, the political and financial crisis had reached a near boiling point. Fresh rounds of multilateral sanctions on banning FDI, lending, and trade were issued, specifically targeting natural resource commodities produced in South Africa.<sup>175</sup> However, “The anti-apartheid sanctions regime was, in addition to being a patchwork of both voluntary and mandatory prohibitions undertaken by a multitude and variety of actors, extremely “leaky”; goods still found their way into and out of South Africa and many white South Africans were able to retain their individual contacts with the rest of the world.”<sup>176</sup>

***b. South African Sanctions Assessment***

Adequacy of Sanctions: Multilateral, government-sponsored sanctions were inadequate to achieve their economic and political objectives alone. South African merchants found ways to bust sanctions with higher-cost import substitution and transshipments through nonparticipating states.<sup>177</sup> Furthermore, evidence indicates that sanctions caused the government of President Botha to intensify repression of nonwhites and dig in harder against perceived foreign interference.<sup>178</sup> Evidence also indicates that unprompted private sector withdrawal of capital and credit was far more economically damaging to South Africa than the public mandates were,<sup>179</sup> but the apartheid regime was able to weather this economic effect as well.

Strengthening of Legitimacy: The most important contribution sanctions made to achieving their political objectives were in delegitimizing the apartheid government and providing much needed legitimacy to the nonwhite oppositionist movement. “The sanctions signaled the extent to which South Africa was isolated in the international community ... although sanctions in one form or another had been in place for a long time, those of the mid-1980s included key South African allies, such as the

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<sup>175</sup> Ibid., 417.

<sup>176</sup> Crawford and Klotz, *How Sanctions Work: Lessons from South Africa*, 12.

<sup>177</sup> Levy, *Sanctions on South Africa: What Did They do?*, 418.

<sup>178</sup> Ibid., 420.

<sup>179</sup> Ibid., 418.

United States, in a nontrivial way.”<sup>180</sup> Black opposition leaders all made statements to the importance of maintaining the sanctions regime during their struggle, which gave their own cause legitimacy.<sup>181</sup>

**Enforcement of Sanctions:** The enforcement of sanctions was satisfactory by participating states, but “sanctions never completely isolated South Africa or white South Africans.”<sup>182</sup> This was due to the ability of the South African business elites to anticipate and adapt to upcoming sanctions.<sup>183</sup> As stated, nonparticipating states took full advantage of multilateral (public) sanctions to adjust international trade, and trade with them somewhat balanced losses from standard trading partners.<sup>184</sup>

**Popularity of Sanctions:** Sanctions against South Africa were almost universally popular due to the normative perceptions of apartheid, as well as to negative perceptions of South African aggression. Popular culture embraced the multilateral sanctions and they were portrayed as a humanitarian cause, strengthening the legitimacy of nonwhite oppositionist movements.

**Structure of the Political Economy:** Sanctions had an important supporting role but were not the primary reason for achieving political goals. The primary reason that political goals were achieved was due to the changing structure of the South African Political Economy; the simultaneous weakening of the white praetorian class and the strengthening of the nonwhite proletariat class due to industrialization and demographics, which ultimately delivered the political goals of economic sanctions in South Africa. Over time, the changing structure of the political economy gave the proletariat class access to education and capital via early reforms in the labor market, which was translated into an unstoppable political movement further strengthened with the legitimacy sanctions bestowed upon it. Other external factors of the political economy that helped achieve both political goals of sanctions was the end of the Cold War and the

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<sup>180</sup> Ibid.

<sup>181</sup> Ibid.

<sup>182</sup> Crawford and Klotz, *How Sanctions Work: Lessons from South Africa*, 12.

<sup>183</sup> Ibid.

<sup>184</sup> Ibid.

withdrawal of Cuban troops from Angola, which further delegitimized the apartheid regime and its necessity of maintaining its hold on power and its military adventures.<sup>185</sup> The communist threat from their neighbors, often overlooked, was a significant external reason why the white praetorian class desired to hang onto power, despite international condemnation of their policies and economic sanctions related to them.<sup>186</sup> Once the communist threat was removed, a powerful incentive for negotiating a share of governmental power, including an ending of apartheid, presented itself.<sup>187</sup>

### 3. Sanctioning Iran

Iranian sanctions, in various forms, have been in place for three decades, undergoing five major rounds of expansions under differing U.S. administrations.<sup>188</sup> The current economic and political goals of sanctions go beyond the nuclear issue and there is still debate among policymakers and analysts as to all the goals sanctions are meant to achieve in Iran.<sup>189</sup> Economic and political goals of current sanctions include:

Taking a moral stance against human rights abuses in Iran; deterring other countries from taking the same nuclear route as Iran; signaling international disapproval [for Iran's foreign and domestic policies]; delaying and disrupting Tehran's nuclear and missile programs; helping the democratic opposition; crippling the country [economically], or at least the government; using sanctions as leverage to open fruitful negotiations on the nuclear issue or perhaps on a broader set of issues [opposition to the Middle East peace process], and; persuading Iran to halt its uranium enrichment efforts.<sup>190</sup>

The structure of the Iranian political economy is fractured and is not composed of a unitary elite like Saddam's Iraq, and certainly not a democracy like South Africa (despite significant segments of the population being excluded from participation in the

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<sup>185</sup> Levy, *Sanctions on South Africa: What Did They Do?* 420.

<sup>186</sup> Ibid.

<sup>187</sup> Levy, *Sanctions on South Africa: What Did They Do?* 420.

<sup>188</sup> Robin B. Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, ed. Robin B. Wright (Washington, D.C: United States Institute of Peace, 2010), 115.

<sup>189</sup> Ibid., 116.

<sup>190</sup> Ibid., 116–117.

government for most of the period of economic sanctions). More detail on the political actors in Iran will be provided in subsequent chapters, but at this point, it is worth mentioning that there is political opposition in Iran to the conservative elites who have the most hold on power, patronage networks, and the security apparatus. Despite early difficulties of enforcement, multilateral economic sanctions are now (circa 2010) having a significant effect on the Iranian economy and are compounding problems resulting from their own internal economic mismanagement. However, as in the other cases, the key to achieving the political goals of sanctions (short of armed conflict) lies in using sanctions to strengthen oppositionist movements in the political economy who will bring about political change, including the political goals of sanctions themselves.

*a. Iranian Sanctions*

UN and worldwide bilateral sanctions on Iran (the latest of which are imposed by Resolution 1929, adopted June 9, 2010) are a relatively recent (post-2006) development. U.S. sanctions, on the other hand, have been a major feature of U.S.-Iran policy since Iran's 1979 Islamic revolution.<sup>191</sup>

The Obama administration's policy, in coordination with Congress, has been to pursue engagement with Iran on the nuclear issue and increase the bite of sanctions incrementally to coerce such a settlement, while not alienating key international sanctions partners for additional sanctions against Iran.<sup>192</sup> Existing sanctions against have been building on each other for many years, to include overlaps with UN and allied states' sanctions regimes to compel Iran to negotiate on multiple issues, especially the nuclear issue.<sup>193</sup>

A brief review of current Iranian sanctions should begin with the declaration of Iran as a State Sponsor of Terrorism in January 1984 and the subsequent

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<sup>191</sup> Katzman, *Iran Sanctions*, 1.

<sup>192</sup> Ibid.

<sup>193</sup> Ibid.

imposition of sanctions to halt foreign aid, dual use (military and civilian) items, and requires the U.S. to oppose international loans or foreign assistance (except in disaster aid).<sup>194</sup>

Sanctions were extended during President Clinton's administration with proscriptions on U.S. participation in Iran's petroleum sector development and investment,<sup>195</sup> and with the Iran-Libya Sanctions Act (ILSA), which "authorized U.S. penalties against foreign firms, many of which are incorporated in countries that are U.S. allies."<sup>196</sup> These extra-territorial sanctions were designed to provide a disincentive for foreign firms to invest in Iran and "became a high profile [foreign policy] issue in U.S. relations with Europe and Russia,"<sup>197</sup> leading to their international unpopularity.

During the Bush administration, the president's authority to impose sanctions in relation to Iran's weapons of mass destruction (WMD) programs was greatly enhanced with the passage of the 2006 Iran, North Korea, and Syria Nonproliferation Act, allowing for the sanctioning of individual persons and corporations and enabling these capabilities in Iran, especially their security services.<sup>198</sup> This supplemented earlier executive orders sanctioning state and nonstate actors providing WMD proliferation and assistance to Iran.<sup>199</sup> Other executive orders during this time froze "assets of firms and individuals said to be involved in Iran's support for terrorism."<sup>200</sup> At this time, the Iran Freedom Support Act of 2006 was also passed, which sought to aid Iranian dissident democratic movements by providing financial assistance with media outlets that "strive for peaceful transformation of the regime and criticized Tehran's nuclear stance."<sup>201</sup>

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<sup>194</sup> Ibid., 29–30.

<sup>195</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 116.

<sup>196</sup> Katzman, *Iran Sanctions*, 1.

<sup>197</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 115.

<sup>198</sup> Katzman, *Iran Sanctions*, 31.

<sup>199</sup> Ibid.

<sup>200</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 116.

<sup>201</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*.

In June 2010, the Obama administration signed the Comprehensive Iran Sanctions, Accountability, and Divestment Act (CISADA). This amended previous U.S. sanctions acts and expanded sanctions “by targeting the supply of refined petroleum products sent to Iran by non-U.S. firms,”<sup>202</sup> and also sanctioned, among other provisions, the sale of “gasoline production related equipment and services to Iran, and to restrict international banking relationships with Iran.”<sup>203</sup> CISADA also strengthened previous efforts by the U.S. treasury department to cut Iran out of the international banking system by banning third country banks that do business in Iran from operating in the U.S.,<sup>204</sup> Following the contested June 2009 election results, CISADA amendments also include measures to use targeted sanctions to promote the domestic opposition in Iran.<sup>205</sup> “Several measures to support the opposition’s ability to communicate, to reduce the regime’s ability to monitor and censor Internet communications and to identify and sanction Iranian human rights abusers, were included in CISADA.”<sup>206</sup>

UN resolutions, which include sanctions against Iran, have been progressing in their frequency, criticism, and international acceptance as well. Six UN Resolutions concerning Iran have been passed since 2006, progressively increasing pressure on Iran to cease its Uranium enrichment and its ballistic missile development.<sup>207</sup>

UN sanctions have progressively targeted officials, government branches and businesses linked to Iran’s nuclear program and military. The resolutions have included travel bans and asset freezes on individuals, front companies, and banks... [they] have also increasingly targeted the Islamic Revolutionary Guard Corps (IRGC)... an alleged driver of the country’s nuclear program.<sup>208</sup>

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<sup>202</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 116.

<sup>203</sup> Katzman and Library of Congress. Congressional Research Service, *Iran Sanctions*, 1.

<sup>204</sup> Ibid.

<sup>205</sup> Katzman and Library of Congress. Congressional Research Service, *Iran Sanctions*, 1.

<sup>206</sup> Ibid.

<sup>207</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 119.

<sup>208</sup> Ibid.

**b. Iranian Sanctions Assessment**

Adequacy of Sanctions: Iranian sanctions, as they exist today, are inadequate to meet their economic and political goals of changing the regime's behavior, specifically with regard to several of the sanctions objectives. Despite their comprehensiveness, the multilateral sanctions that exist today do not appear to be altering the regime's behavior to negotiate seriously regarding its nuclear enrichment issue, or other issues, to include: ending of human rights abuses and support for terrorism; delaying or disrupting their long range missile programs; significantly helping the democratic opposition; and kick-starting nuclear negotiations.<sup>209</sup>

Furthermore, since there is no precise agreement among U.S. officials on the specific political goals of sanctions, assessing their economic effects relative to political goals is difficult from the outset.<sup>210</sup> Sanctions have slowed down Iranian access to global finance and foreign investment, as well as some of Iran's weapons procurement and development.<sup>211</sup> "U.S. officials believe that Iran's economy will inevitably begin to suffer as U.S. and partner strategy shuts Iran out of the global financial system, raises the costs for Iran of financing its transactions, and causes international firms to exit Iran."<sup>212</sup> Since there is only anecdotal evidence that (counter-proliferations type) sanctions are physically slowing down Iran's nuclear program<sup>213</sup> and that the economic effects from sanctions (causing substantial foreign capital flight and reduction in energy sector development) are still not changing Iranian behavior, sanctions must be assessed as inadequate. "There is a consensus that U.S. and UN sanctions have not, to date, accomplished their core strategic objective of causing a demonstrable shift in Iran's commitment to its nuclear program."<sup>214</sup> Additional goals of sanctions, specifically to promote domestic opposition in Iran, are also inadequate due to the political and financial

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<sup>209</sup> O'Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 88; Katzman and Library of Congress. Congressional Research Service, 39.

<sup>210</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 118.

<sup>211</sup> O'Sullivan, *Shrewd Sanction: Statecraft and State Sponsors of Terrorism*, 88.

<sup>212</sup> Katzman, *Iran Sanctions*, 46.

<sup>213</sup> Ibid.

<sup>214</sup> Ibid.

weakness of opposition groups in Iran. Should such efforts fail, it would lead to greater diplomatic difficulties with the conservative clerics now in control—possibly perceived as another Operation Ajax circa 1953, and should such efforts succeed—without a strong constituency to provide financial and political support to the oppositionist group, they would not last long.<sup>215</sup>

Recent changes to the government’s subsidies program, specifically the phasing out of gasoline and other energy subsidies by 2015, is not assessed to be linked to sanctions despite some literature attributing the change to sanctions potential mitigation. Subsidies have consumed a large percentage of Iran’s GDP (25 percent) in 2009, and past efforts to curb these subsidies have met with a political backlash—including riots, unrest, and attacks on energy infrastructure.<sup>216</sup> Ahmadinejad’s successful campaign to end subsidies—and transfer their wealth in the form of cash payments to the poor—have spiked inflation, eroding the purchasing power of his own constituency that he was trying to help,<sup>217</sup> as well as weakening the overall competitiveness of Iranian industry, which depends on subsidies for cheap energy inputs.<sup>218</sup>

Strengthening of Legitimacy: Economic sanctions are having a mixed effect confirming the legitimacy of the clerical conservative actors who currently control the government in Iran. Domestically, the conservative factions’ attempts to use economic sanctions to their advantage, and confirm the legitimacy of their government, appear to be working across the broader Iranian society, due to their control of the media and portrayal of their nuclear program as peaceful. Internationally, however, continued sanctions and UN resolutions are weakening their legitimacy. “Proposals [of multilateral sanctions and UN resolutions] to target the Revolutionary Guards for sanctions... represent one facet of the trend toward measures that undermine the legitimacy of Iran’s regime and support Iran’s domestic opposition.”<sup>219</sup>

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<sup>215</sup> O’Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 93.

<sup>216</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 104.

<sup>217</sup> Ibid., 105.

<sup>218</sup> Ibid., 106.

<sup>219</sup> Katzman, *Iran Sanctions*, 32.



Enforcement of Sanctions: Enforcement of Iranian sanctions is stronger internationally than it has ever been, but Iran is utilizing significant gaps to maintain the status quo. “Implementation appears to be somewhat less complete in Iran’s immediate region, perhaps because its neighbors do not want confrontation with Iran and are hesitant to disrupt traditional relationships among traders and businessmen in the region.”<sup>220</sup> The United Arab Emirates (U.A.E.) is Iran’s fifth largest trading partner, holding 8 percent of its foreign trade.<sup>221</sup> U.S. diplomatic efforts with the U.A.E. have resulted in increased sanctions enforcement there, raising the costs of legitimate imports,<sup>222</sup> but smuggling persists. Outside of Iran’s regional neighborhood, China’s appetite for energy security can only be satisfied by Iran, and this relationship undermines American sanctions.<sup>223</sup> China is Iran’s second largest trading partner (15 percent of foreign trade) behind the European Union (EU) at 21 percent.<sup>224</sup> The U.S.’s own dependence on Chinese trade relations precludes it from utilizing strict sanctions measures against Chinese firms involved in trade with Iran, despite some recently demonstrated examples.<sup>225</sup> The Republic of Korea, Iran’s sixth largest trading partner at 7 percent of foreign trade, has also further increased its economic ties to Iran.<sup>226</sup>

Popularity of Sanctions: Iranian sanctions adopted by the UN have finally gained near-universal international support, at least in spirit—as room for improvement exists in sanctions’ practical application. European allies have grown increasingly concerned with Iran’s behavior and the nuclear impasse.

U.S. allies have generally supported and joined the Obama administration’s sanctions toward Iran, in part because the approach is perceived as not purely punitive, and in part because their own concerns about Iran’s nuclear advancement have increased ... as of 2010, an

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<sup>220</sup> Ibid.

<sup>221</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*.

<sup>222</sup> Brian Murphy, “Iran’s Gateway in Dubai Highlights Sanctions’ Bite,” *Associated Press* (1 February 2011), 5 November 2011.

<sup>223</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*.

<sup>224</sup> Ibid.

<sup>225</sup> Ibid.

<sup>226</sup> Ibid.

unprecedented degree of global consensus has emerged on how to deal with Iran. There is a degree of consensus among experts that many countries, not only allies of the United States, are complying with the provisions of UN sanctions.”<sup>227</sup>

China continues to voice its sanctions concerns, and does not support sanctions outside those adopted by the UN.<sup>228</sup> “As a UNSC member, China traditionally has spared no effort to emasculate UNSC resolutions so that they cannot create any problems for the developing cooperation between [China and Iran].”<sup>229</sup>

Structure of the Political Economy: The structure of the Iranian political economy is the ultimate inhibitor to sanctions effectiveness. As will be shown in the next chapter, the conservative factions’ control over the sources of economic wealth in Iran, and the lack of access to wealth by reformist actors are ultimately preventing the accomplishment of the goals of economic sanctions. Sanctions, as they currently exist, are having an economic impact on Iran and the actors who control this economy, but are not adequately promoting the ability of opposition groups to gain sources of wealth that could be utilized to challenge the more conservative factions for control of government. As previously discussed, incomplete sanctions enforcement is further inhibiting sanctions effectiveness of limiting wealth from reaching the entrenched conservative actors in the political economy.

## C. CONCLUSION

This chapter has examined some methods for analyzing sanctions variables for success and failure, and reviewed specific examples of historical sanctions cases, and drawn conclusions as to reasons for their failures and successes. The role of the actors in the political economy must be taken into account when designing smart sanctions, with the goal of using sanctions to empower oppositionist movements to challenge the established actors who are resistant to the political goals sought with sanctions.

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<sup>227</sup> Katzman *Iran Sanctions*, 37.

<sup>228</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*.

<sup>229</sup> *Ibid.*

Iraqi sanctions, despite being in place for a decade, failed due to their inability to permanently link oppositionist movements to needed capital and constituency bases to challenge Saddam. The sanctions did achieve their economic goals of hurting the Iraqi economy, but Saddam's hold on power in Baghdad was not overcome. Conversely, South African sanctions were viewed as successful due to their ability to confer legitimacy on oppositionist movements, to establish a power base (among the industrial proletariat) in the political economy. The nonwhite oppositionist actors used this newfound capital to organize into an unstoppable political force that was eventually able to overcome the established actor, the white Afrikaners in Pretoria.

Iranian sanctions have an opportunity to work due to the fragmented structure of the political economy, with multiple actors, each with their own capital base. However, current sanctions are inadequate to support this kind of growth of an opposition—due to their primary focus on blunting the economic base of the conservative actors (IRGC, etc.), and due to outside states continuing to enable the conservative actors to maintain their power base by continuing their substantial trade.

Economic sanctions against Iran also have primary and secondary consequences, which set in motion further linked events within the political economy. The most glaring example is the growth of the IRGC into economic endeavors as a result of sanctions and the limitations of the private sector to accomplish reconstruction and defense-related production following the Iran-Iraq war.<sup>230</sup> Other examples include the growth of smuggling networks, due to sanctions, and their cooption by political actors as a constituency. This makes assessments of sanctions' effects more complicated, and political and economic sanctions' analysis more difficult to determine.

A further examination of Iranian actors is therefore necessary to flesh out this argument further, as an understanding of the power bases upon which an actor relies is necessary. This will be the focus of the next chapter.

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<sup>230</sup> Richard L. McKnight, *Sanctioning Success?: Assessing the Role of Sanctions in the Militarization of Iran* (Monterey, California: Naval Postgraduate School, 2010), 28.

### III. CURRENT ACTORS OF THE IRANIAN POLITICAL ECONOMY

To Western eyes, Iran appears to be a monolithic, conservative clerical regime that has a unified political agenda. Its conservative leaders, whose abrasive and controversial comments get the most airplay, appear to represent the views of the entire polity. By peeling back the layers of rhetoric and the selective sampling of comments by Western media and domestic lobby groups, a different picture is painted. This picture portrays a regime that has split into four broad political actor elite groups, each with its own constituencies and patronage networks that provide the actor elites political support.

Khomeini's doctrine of Velayat-e Faqih, which was built on earlier works of Islamic socialist economics, espoused a panacea for all of Iran's political and economic problems.<sup>231</sup> Therefore, once in power, he and his supporters did not envision (and would not tolerate) more than one actor group (termed, the radicals)<sup>232</sup> participating in government and the political economy. The radicals, led by Ayatollah Khomeini, "called for a classless society, export of the Islamic revolution, and a socially and economically interventionist state."<sup>233</sup> His regime thus devolved into a nationalized state-centric economy, reliant upon petrochemical exports to provide for government revenues to maintain employment and patronage networks, while relying on an ever increasingly draconian security apparatus to suppress with political dissent. But among the elite, differences of opinion and policy emerged that would eventually form into their own actor factions.

Though the Islamic Republic curtailed the liberty of Iranian society and especially its political opponents, the internal culture of the political elite was sufficiently free to allow different opinions to be played against the others. Combined with a constitutional framework that counterbalances

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<sup>231</sup> Shaul Bakhash, *The Reign of the Ayatollahs: Iran and the Islamic Revolution* (New York: Basic Books, 1984), 167.

<sup>232</sup> Kjetil Bjorvatn and Kjetil Selvik, "Destructive Competition: Factionalism and Rent-Seeking in Iran," *World Development* 36, no. 11 (2008), 2316.

<sup>233</sup> Ibid.

mutually independent institutions, this culture of disagreement [eventually] led to the emergence of four main political factions.<sup>234</sup>

Upon Khomeini's death in 1989, the new elite actor factions began to openly emerge in politics for the first time, challenging the radical actor faction for control of government and of the political economy. These actor groups had to develop their own constituencies—complete with the traditional trade-off of political support for patronage—to survive the life or death world of Iranian politics. “Because the state is the main source of income, groups compete to occupy governmental positions and gain influence in society.”<sup>235</sup> Within a few years of Khomeini's death, the radical faction would disappear and evolve into newer actor groups—as loyalties and beliefs of its members changed over time and issue. Iran's key political positions for 25 years of its revolutionary history were held by clerics, and only since 2005 have laymen played a significant part—due mostly to the fracturing of political discussion among the clerical elite themselves, as more reformist politicians grew more and more popular among the polity. Ayatollah Khomeini was revered as a modern day Imam and was considered the greatest among the clerical equals of his day (although devout Shia have stated the use of the Imam title was an affectionate nickname, as the last true Imam is still in occultation and the devout are awaiting his return). Upon his death, new Supreme Leader Khamenei's clerical peers did not give this same amount of deference to him,<sup>236</sup> as their religious credentials often exceeded his and they had shared the same educational and revolutionary experiences. Reformist politicians, often with more religious credentials and public support, were a significant threat. The emergence of the neoconservative actors as a political actor has largely eliminated this threat.

Ahmadinejad's election in 2005 was conditioned by the rise of the military-security second stratum [neoconservatives] of Iran's new political class and reflects its aspirations. It is as a representative of the hardliners

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<sup>234</sup> Kjetil Bjorvatn and Kjetil Selvik, “Destructive Competition: Factionalism and Rent-Seeking in Iran,” *World Development* 36, no. 11 (2008), 2316.

<sup>235</sup> Kazem Alamdari, “The Power Structure of the Islamic Republic of Iran: Transition from Populism to Clientelism, and Militarization of the Government,” *Third World Quarterly* 26, no. 8 (2005), 1290.

<sup>236</sup> Said Amir Arjomand, *After Khomeini: Iran Under His Successors* (New York, New York: Oxford University Press, 2009), 149.

from the second stratum that he has contested the pragmatist and the reformist definitions of Khomeini's heritage in seeking to articulate the consciousness of this new political class and its aspiration to rule Iran indefinitely.<sup>237</sup>

This chapter will closely examine these actors in the Iranian political economy, determining their strengths, weaknesses, interactions, and constituencies. This analysis will allow for a renewed analysis on the impact of economic sanctions in the final chapter, and how better to tailor them. In conducting this analysis, this chapter will attempt to validate the first hypothesis (*Analysis of sanctions effects should be actor centric*) and second hypothesis (*Sanctions must alter the current asymmetric balance of power in the Iranian political economy to achieve their political objectives*).

## **A. IRANIAN ACTORS AND INTERESTS**

As previously stated, the Iranian political system is characterized by highly factionalized actors with separate constituencies, each pursuing differing agendas in the political economy.

The factional political system has created room for discretion and arbitrariness in the design and implementation of rules and regulations. This lack of state autonomy has stimulated rent seeking, favoring well connected public and quasi-public enterprises and hindering private investment.<sup>238</sup>

This chapter will examine each actor in detail to determine their interests, and potential vulnerabilities to economic sanctions that could produce political results. The overall political system is also examined to determine each actor's interactions with each other and identify possible areas of conflict between them. "At its core, the Iranian system is closed, secretive, informal, and clannish ... also intensely fractured and multipolar, in some cases by accident, in others by bureaucratic design."<sup>239</sup> The actors' disagreements

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<sup>237</sup> Said Amir Arjomand, *After Khomeini: Iran Under His Successors* (New York: Oxford University Press, 2009), 149.

<sup>238</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2314.

<sup>239</sup> Jerrold D. Green et al., *Understanding Iran* (Santa Monica, CA: Rand Corp., 2009), 6.

are often issue dependent and require mediation (often by the supreme leader) to find common ground and move forward with policy.<sup>240</sup>

The nuclear issue remains as controversial among the Iranian actors as it does internationally. “The weapons component of the program has never been debated or acknowledged ... since 2009, factions take positions that do not reflect their real preferences, mainly to thwart political rivals.”<sup>241</sup> The more conservative actor groups accuse the reformists of selling out nuclear enrichment rights,<sup>242</sup> and the reformists criticize the conservatives’ “nuclear policy as provocative and costly to Iran, despite the supreme leader’s explicit support.”<sup>243</sup> The larger public supports the program due to the way it is presented to them—as a peaceful means to obtain energy independence and make scientific progress—while asserting Iranian sovereign rights to enrich Uranium.<sup>244</sup> “The program has not been subjected to informed debate or public discussion about its ultimate goals, the costs, and the relationship with Iran’s other objectives. Consensus [among the actors] ends where specifics begin.”<sup>245</sup> “Rival factions ... criticize the nuclear programs costs and centrality to Iran’s development goals. Iran’s nuclear program had become a domestic political football.”<sup>246</sup>

## **1. Conservatives and Their Constituents**

Current Supreme Leader Ayatollah Ali Khamenei is the nominal head of this actor group, which is constituted by the elite clergy (the patrons), with a political constituency, very broadly speaking, of the lower clergy and the bazaar (the clients).<sup>247</sup> Most state institutions in Iran are controlled by this group, who also control a majority stake in the political economy.

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<sup>240</sup> Ibid.

<sup>241</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 85.

<sup>242</sup> Ibid.

<sup>243</sup> Ibid.

<sup>244</sup> Ibid., 83.

<sup>245</sup> Ibid.

<sup>246</sup> Ibid.

<sup>247</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2317.

Economic sanctions, as they exist today, will fail to alter the behavior and control of the government of the conservative actor group. The conservative actors are cushioned by the redundancy of income the conservatives enjoy from the bonyads and their redundant control over differing economic sectors, while also continuing to receive political support from the bazaaris who are still able to circumvent import sanctions via their smuggling networks. These two powerful constituencies have provided the conservative actor group its base since the revolution, as well as their ability to play off the other actor groups against each other to maintain control, despite a worsening economic situation and decreasing legitimacy.

*a. Interests of the Conservatives*

The conservatives were the first group to emerge as a dissenting voice to the radicals of the 1980s, who favored “private property rights, revolution in one country, and traditional Islamic jurisprudence over state-led remaking of society.”<sup>248</sup> This actor group became the preeminent group in Iranian politics following the abandonment of the radical party after Khomeini’s death, and will remain the dominant party for the foreseeable future due to its hold on majority memberships within the reform-busting nonelected institutions such as the Guardian Council and Expediency Council (due to direct appointments from the supreme leader). The conservatives are also in a position to act as arbiter among the other parties and often use their control of the highest offices to ensure they maintain control of other nonelected political institutions. As the oldest and most entrenched actor group in the Iranian polity, they balance out the political landscape and other actors (allowing them a lesser degree of access to rents and political offices) to prevent greater unrest against their own political hegemony.<sup>249</sup> The conservative actors’ interests, therefore, are to: maintain their central political position within the state, keep an entrenched majority in the important nonelected institutions in Iran (where power ultimately resides); resist globalizing economic policies that they cannot co-opt, control, or profit from and; maintain the independence of the clergy and their bonyads from

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<sup>248</sup> Ibid., 2316.

<sup>249</sup> Ibid., 2317.



populist movements to maintain their patronage networks. “Their primary concern is not a U.S. military invasion, but rather a political and cultural campaign to undermine theocratic rule through a ‘soft’ or ‘velvet’ revolution.”<sup>250</sup> This group, like all groups, relies on access oil sector rents to provide patronage to its constituents.

The conservatives strongly support the continued enrichment of Uranium, despite international opposition, while denying this enrichment has any military connection (i.e., enrichment to weapons grade). Supreme Leader Khamenei’s statements remain ambiguous, but it is clear that this is intentional. “He has rarely pronounced on the nuclear program except in generalities. He insists that there is an unspecified fatwa against the development of nuclear weapons, but has supported policies that make it impossible to verify this fatwa in practice.”<sup>251</sup> A nuclear weapon, however, would provide his regime with a significant measure of security against external intervention. “For Khamenei, the nuclear program has come to embody the revolution’s core themes: the struggle for independence, the injustice of foreign powers, the necessity of self-sufficiency, and Islam’s high esteem for the sciences.”<sup>252</sup> Historical precedent also lends credence to this idea; recent reports indicate it was then President Khamenei who, in April 1984, secretly announced to top Iranian officials the reactivation of Iran’s nuclear program (based upon guidance from then Supreme Leader Khomeini),<sup>253</sup> and now he, as the current supreme leader, “has ultimate say over Iran’s nuclear program, and all major decisions on the nuclear issue require his approval.”<sup>254</sup> Since Iran has not agreed to comply with the requirements of the Nuclear Non-Proliferation Treaty (NPT) and disclose its enrichment activities, his position can be inferred. Constituents of the conservatives (lesser clerics and the bazaaris) who have an interest in keeping them in power, also generally support this policy. Lesser clerics support it due to the security it provides their patrons, and thus, their positions. The bazaaris would theoretically support

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<sup>250</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 12.

<sup>251</sup> Ibid., 85.

<sup>252</sup> Ibid., 13.

<sup>253</sup> Ibid., 78.

<sup>254</sup> Ibid., 80.

any policy that provides them a better business environment, and as will be shown, there are indications that sanctions related to the nuclear issue are increasing their business costs. But the historical tie between the bazaaris' lobby groups and the conservatives go deep, and as will be shown, the most important bazaaris are allowed access to profitable Western goods largely by connections to their clerical elite patrons, who in many cases, have become family.

*b. Economic Assets and Constituents of the Conservatives*

The conservatives are unique actors in that their constituents control the hundreds of bonyads across the country (usually headed by lower level clerics appointed by the supreme leader or other elite cleric), and these constituencies provide rents of their own. "Many bonyads seem like rackets, extorting money from entrepreneurs. Besides the biggest national outfits, almost every Iranian town has its own bonyad, affiliated with local mullahs."<sup>255</sup> Successful local entrepreneurs who fail to do exclusive business with and/or provide bribes to their local bonyad leadership can find themselves before a judge explaining a trumped up religious infraction.<sup>256</sup> The bonyads are the Iranian economy's dominating revenue generating entity outside the oil sector,<sup>257</sup> mushrooming in size and scope of operations over the years. "Monopolizing wide swaths of trade and business... [bonyads] alone control 25 percent of GDP."<sup>258</sup> The conservative actor group receives exclusive rents from these organizations. In return, the clerical elites provide patronage to their lesser clerical constituents (who nominally head each bonyad) in the form of legislation and orders to other institutions that prevents bookkeeping scrutiny and emasculates their private sector competition. As patronage disguised in religion, the bonyads—as religious foundations—are "exempted from taxes and government control...

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<sup>255</sup> Paul Klebnikov, "Millionaire Mullahs," *Forbes Magazine*, 21 July 2003, <http://members.forbes.com/global/2003/0721/024.html>.

<sup>256</sup> Ibid.

<sup>257</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2317.

<sup>258</sup> Robert Looney, "The Iranian Economy: Crony Capitalism in Islamic Garb," *The Milken Institute Review*, no. First Quarter, 2006 (28 March 2006), 35.

[and] also receive direct transfers through the budget.”<sup>259</sup> The bonyads connections to the elite clerics have allowed them to “enjoy preferential access to bank credit, hard currency, government licenses and lucrative contracts, thus crowding out more productive private sector activities.”<sup>260</sup> Banking and finance sectors of the economy are also still controlled by this actor with government ownership at 89 percent of bank assets,<sup>261</sup> an outgrowth of the nationalizations during the revolution. The perception of clerical corruption across Iranian society is widespread, given the clerical access to “hefty government stipends, as well as other exclusive and profitable privileges,”<sup>262</sup> while the rest of the Iranian society suffers a net decreasing standard of living (as represented by economic growth per capita hovering just in the negative since the revolution, (–0.1 percent)).<sup>263</sup>

The other constituency of the conservatives is the bazaar, whose relationship with the elite clergy has endured since joining forces during the 1979 revolution to oust the Shah. While the bazaaris are not a monolithic group, and some certainly are aloof from politics, analysis of this group’s historical lobbying places them in the conservative camp.

The alliance between mosque and bazaar had historical roots. It was reinforced in the 1970s because, despite their newfound wealth, the bazaar classes harbored numerous grievances against the policies pursued by the Shah’s government and also against the new industrial and entrepreneurial elite whose interests these policies helped to promote.<sup>264</sup>

This relationship was further cemented during Rasfajani’s presidency, when he “attempted to organize the pro-capitalist entrepreneurs in both industry and trade,

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<sup>259</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2317.

<sup>260</sup> Looney, *The Iranian Economy: Crony Capitalism in Islamic Garb*, 35.

<sup>261</sup> Henry and Springborg, *Globalization and the Politics of Development in the Middle East*, 304.

<sup>262</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 28.

<sup>263</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2315.

<sup>264</sup> Bakhash, *The Reign of the Ayatollahs: Iran and the Islamic Revolution*, 191.

offending traditionalist merchants.”<sup>265</sup> This clever (attempted) reorganization of political patronage, away from the clerics, caused a backlash, and “in order to avoid a further assault on their power, bitter fundamentalist merchants were encouraged to join forces with senior fundamentalist ‘ulema,’ or clergy, in opposing Rafsanjani’s cultural and economic policies.”<sup>266</sup> Over time, some of these relationships between influential clergy and bazaaris have been cemented by intermarriage, leading to the awarding of monopoly licenses and other influential governmental positions.<sup>267</sup> “The [conservative] regime is a religious oligarchy related by blood and financial ties to the bazaar and merchant class.”<sup>268</sup> The term bazaaris is used to describe the “heterogeneous commercial class located in historical urban centers.”<sup>269</sup> It is important to note that not all bazaaris have connections to the regime, and in recent years, this constituency group has lost some of its previous political influence. This is due to several factors, the primary one of which is the slow and unstoppable force of globalization. With the slow but steady growth of air-conditioned shopping malls near residential areas, coupled with a shift in consumer tastes, specifically the bulging youth population in Iran, who prefer Western styles and products (even Asian copies), “fewer wealthy Iranians living far from downtown are willing to travel to the bazaar to make major purchases.”<sup>270</sup>

As a client member within the conservative camp, the bazaaris lobby their patron clerics to open up trading opportunities, specifically for “more laissez-faire policies that would remove state tariffs and regulations on trade.”<sup>271</sup> This lobbying is carried out via two influential business organizations (that share memberships)<sup>272</sup> in

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<sup>265</sup> Hossein S. Seifzadeh, “The Landscape of Factional Politics and Its Future in Iran,” *The Middle East Journal* 57, no. 1 (2003), 61.

<sup>266</sup> *Ibid.*, 61.

<sup>267</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 109.

<sup>268</sup> Jahangir Amuzegar, “Iran’s Economy and the US Sanctions,” *Middle East Journal* 51, no. 2 (1997), 39.

<sup>269</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 108.

<sup>270</sup> *Ibid.*, 109.

<sup>271</sup> *Ibid.*, 110.

<sup>272</sup> *Ibid.*

Iranian politics: the Islamic Coalition Association (ICA), and the Society of the Islamic Associations of Tehran's Guilds and Bazaar. The ICA originated in the bazaar in the 1960s as an oppositionist movement against the Shah (supporting Khomeini), and "after 1979, ICA members were placed in high government posts and took staunchly conservative positions in factional battles."<sup>273</sup> Evidence of this patronage relationship can be seen during the green movement protests of June–July 2009, where the bazaaris were especially quiet, not taking part in the protests against the clerical leadership and their perceived fraud and corruption.<sup>274</sup> Since bazaaris would presumably form the nucleus of an emerging middle class in Iran, it would seem plausible that they would be among the first to protest an opaque and corrupt government, but this did not happen. Instead, their most vocal activity is to continue to lobby for the removal of tariffs and regulations that inhibit the imports and exports of finished goods.<sup>275</sup> Possible further evidence of this patron-client union can be seen with the inclusion of the bazaaris and their employees into the generous Social Security Organization's self-employed pension program,<sup>276</sup> passed in September of 2004 as part of the 4th (5 year) Development Plan (2004–2009), shortly after the conservatives took back control of the Majles, in May of that year.

Richard McKnight argues, very persuasively in his thesis, that economic sanctions over the last two decades have resulted in the creation of a shadow smuggling economy controlled by the IRGC, leading to its further entrenchment in the political economy. His research indicates smuggling networks have grown up in Iran, bringing in Western goods (through IRGC controlled ports and airports) that avoid paying the high state tariffs and benefiting their affiliated business organizations.<sup>277</sup> That the bazaaris are also involved in the smuggling of Western goods into Iran is an almost certainty. Seventy

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<sup>273</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 108.

<sup>274</sup> "IRAN: Future Opposition Leaders may be More Radical," *Oxford Analytica Daily Brief Service* (28 April 2010), 1.

<sup>275</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 110.

<sup>276</sup> Ibid.

<sup>277</sup> McKnight, *Sanctioning Success? [Electronic Resource]: Assessing the Role of Sanctions in the Militarization of Iran*, Naval Postgraduate School (U.S.) 49.

percent of foreign clothing for sale in Iran is smuggled in<sup>278</sup> and the bazaaris maintain connections with Iranian expatriates in the U.A.E. to obtain the most fashionable Western products.<sup>279</sup> Direct IRGC linkages to specific bazaaris are unknown, as is the specific involvement of the bazaaris to their own independent smuggling operations. What is known is that there is tension between the bazaar-founded ICA and the neoconservatives in government, as evidenced by the closing of many bazaars across Iranian cities to “protest over the Ahmadinejad government’s attempts to raise and collect more taxes from bazaar shops ... [which] resulted in the government backing down to the demands of the bazaaris.”<sup>280</sup> In other words, another political actor in the Iranian political economy (the neoconservatives) had tried and failed to weaken the constituency of another actor group (the conservatives), likely due to top-cover from their political patrons and push-back from the constituency itself.

*c. Behavior and Motives of the Conservatives*

Conservatives are concerned about reforms that will undermine their hold on power, the retaining of which is their highest motive.<sup>281</sup> Therefore, conservatives behave in a manner towards other political actors that ensures they remain preeminent, and other factions’ levels of influence are subordinate and balanced with each other. “By making sure that politicians from different factions are appointed to different institutions, the [Supreme] Leader undermines challengers to his own predominant position and especially counterbalances the power of the systems number two—the president.”<sup>282</sup> Conservatives discredit reformists in order to handicap their legitimacy and appeal—often by accusing their reformist policies as being Western in origin,<sup>283</sup> especially economic ones that would create true private sector reforms. Conservatives continue to tow the party line that the revolution and its ideals are sacred, and regard any discourse

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<sup>278</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 110.

<sup>279</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 110.

<sup>280</sup> Ibid., 109–110.

<sup>281</sup> Seifzadeh, *The Landscape of Factional Politics and its Future in Iran*, 65.

<sup>282</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2317.

<sup>283</sup> Seifzadeh, *The Landscape of Factional Politics and Its Future in Iran*, 65.

otherwise as a threat—especially their concept of a religious welfare state that deems “society’s underprivileged must remain at their religious mercy.”<sup>284</sup> Conservatives have also not altered their approach of using the most brutal methods of force to suppress dissent,<sup>285</sup> for which they have increasingly relied on the neoconservatives and their security force constituents to provide.<sup>286</sup> Conservatives also rejected and suppressed the proposed economic reforms of the pragmatists when their own share of the political economy was threatened.

Conservatives, especially those entrenched in the bonyads, bitterly and successfully opposed a home-grown structural adjustment program that President Ali Akbar Hashemi Rafsanjani [of the Pragmatist actor group] had launched shortly after the death of Ayatollah Khomeini.<sup>287</sup>

Banking and finance sectors of the economy are also still controlled by the conservative clerics, an outgrowth of the nationalizations during the revolution, with government ownership of 89 percent of bank assets.<sup>288</sup> Cheap credit has been one of this actor’s preferred means of distributing patronage. Access to this credit is preferential and based upon the client’s connections to the actor who can influence the state banks. Money is often used for purposes other than intended, sometimes not repaid at all, often without any consequences to the client receiving the loans.<sup>289</sup> Iran is fully integrated into the global financial system;<sup>290</sup> therefore, multilateral efforts to shut Iran out of the international banking system have significantly “complicated Tehran’s ability to engage in International business, commerce, and finance.”<sup>291</sup> There are reports that Iranian bazaari merchants face significant cost increases for conducting business through Dubai, which requires significant amounts of credit, if they are able to get financing or shipping

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<sup>284</sup> Seifzadeh, *The Landscape of Factional Politics and Its Future in Iran*, 63.

<sup>285</sup> Ibid.

<sup>286</sup> Ibid.

<sup>287</sup> Henry and Springborg, *Globalization and the Politics of Development in the Middle East*, 306.

<sup>288</sup> Ibid., 304.

<sup>289</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2318.

<sup>290</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 123.

<sup>291</sup> Ibid.

availability to avoid sanctions at all.<sup>292</sup> The president of the Iranian chamber of commerce “acknowledged in October [2010] that sanctions were driving up the costs of imports by 15 to 30 percent.”<sup>293</sup> Control of the banking sector has, therefore, been a source of conflict as other actors (specifically, the neoconservatives) have attempted to replace the banks’ conservative leadership with their own loyalists to distribute patronage to preferred clients.<sup>294</sup>

## **2. Neoconservatives and Their Constituents**

The neoconservatives are a group of actors who emerged as a reaction to the (attempted) reform period of President Khatami. They are an elite group of mostly war veterans who cut their teeth as patriotic foot soldiers in the security and military services during the revolution and subsequent war with Iraq. This group is nominally headed by President Ahmadinejad and other elite members of the security forces and, broadly speaking, their constituent clients are the lower ranks of the security forces, specifically the IRGC and Basij, and include other active and retired officers in the military (including veterans), and the socially deprived.<sup>295</sup> While the security forces have existed as a pillar of the regime since the revolution, they have truly become an independent force since the election of Ahmadinejad and their marked expansion in their own right into the political economy.

Ahmadinejad’s election in 2005 was conditioned by the rise of the military-security second stratum of Iran’s new political class and reflects its aspirations ... [their] alternative definition of Khomeini’s heritage highlights what was left unclaimed by the previous two groups [pragmatists and reformists] of the children of the Islamic revolution: populism, social justice, and unflinching loyalty to the martyrs of the revolution and war.<sup>296</sup>

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<sup>292</sup> Murphy, *Iran’s Gateway in Dubai Highlights Sanctions’ Bite*, 5 November 2011.

<sup>293</sup> Murphy, *Iran’s Gateway in Dubai Highlights Sanctions’ Bite*, 5 November 2011.

<sup>294</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2318.

<sup>295</sup> Ibid., 2317.

<sup>296</sup> Arjomand, *After Khomeini: Iran Under His Successors*, 149.



Perhaps the best way to describe the rise of this group of actors is by pointing out that the deeply conservative (nonclerical) elite security service veterans, seeing the decadence and failures of the clerics to contain the reformist movements of the late 1990s, took it upon themselves to ensure the survival of the ideals of the Islamic Revolution. This was done by a soft usurpation of economic and, later, political power from the clerics, while remaining nominally loyal to one—Supreme Leader Khamenei—whose own weak religious credentials (and the eroding of the legitimacy of the clerical leadership in general) have meant this power shift in the political economy was a fait accompli.

Ahmadinejad [as one of the neoconservative elites] has been able to build a base of support among the very constituencies on which Khamenei depends: The Revolutionary Guards, the paramilitary forces, the security agencies and the judiciary ... they are claiming an increasingly larger role in political affairs.<sup>297</sup>

Economic sanctions against this actor group, as they currently exist, are counter-productive in weakening their control of government or altering their policies, given the clout of their security clients and the political and financial support they can generate via their economic enterprises and control of smuggling.

The Guards' reported involvement in illicit economic activities may also cushion them from the full effects of sanctions. Ironically, tougher sanctions would undoubtedly further damage Iran's overall economy, but may strengthen the very force now driving their national security policies, including their nuclear program."<sup>298</sup>

In other words, sanctions must be designed in a way to weaken this actor's hold on political power, versus punishing this actor for bad behavior.

The IRGC also has a clear economic interest in a general sanctions regime, which has removed foreign direct investments in Iranian businesses and removed foreign competitors from the Iranian oil and natural gas market, thereby helping the IRGC expand its economic clout through the seizure of major projects.<sup>299</sup>

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<sup>297</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 19.

<sup>298</sup> Ibid., 60.

<sup>299</sup> Alfoneh, "All the Guard's Men: Iran's Silent Revolution," 78.

Current sanctions also weaken the bazaar and the pragmatist-connected technocrats and, “as these players retreat from the Iranian market, the IRGC not only fills the economic vacuum they leave behind, but also gains their political influence.”<sup>300</sup>

*a. Interests of the Neoconservatives*

The neoconservatives, while pledging loyalty to the supreme leader, believe the clerics of the conservative actor group have been lax in their leadership and have strayed from the original ideological values of “strict moral enforcement, social justice, and anti-imperialism.”<sup>301</sup> This actor group’s interest is to usurp control from other actor groups (to include, specifically, the conservatives) in “all social, political, and economic realms of the Islamic Republic.”<sup>302</sup> Due to the nature of the Islamic Republic as a rentier state, this competition required them to grow and develop their own patronage networks. The IRGC, other security services and poor voting constituents have filled this void as clients to the neoconservative patrons. The neoconservatives swept to governmental power from 2003–2005 with the help of their clients.

In the presidential elections of June 2005, the IRGC and the Basijis perfected the new function of bringing [poor] voters to the ballot box, something they had begun experimentally in the municipal elections of 2003, and the Majles elections of 2004. The 2005 presidential elections could indeed be accurately described as their first electoral coup d’état.<sup>303</sup>

These same security clients have also, historically, assisted the regime by effectively putting down political dissent. As recently as the February 11, 2010, planned green movement protests, which were to coincide with the anniversary of the Islamic revolution, “the advance crackdown [by security forces] was so pervasive that leaders of the movement called it off. Public demonstrations were basically over.”<sup>304</sup> Similarly, the

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<sup>300</sup> Ibid.

<sup>301</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2316.

<sup>302</sup> Alfoneh, “All the Guard’s Men: Iran’s Silent Revolution,” 77.

<sup>303</sup> Arjomand, *After Khomeini: Iran Under His Successors*, 151.

<sup>304</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 43.

1999 student protests, starting at Tehran University and spreading to other cities across Iran, protesting the curbing of press freedom, were similarly shut down by the threat of IRGC intervention.<sup>305</sup>

The neoconservative growth in political power has been a source of tension between the conservatives and neoconservatives, of late, as the neoconservatives have moved to take over more political offices and political institutions of government to further expand their own bases of support and implement their own domestic and foreign policies. This political conflict was best seen in June of 2011 with a widening split between President Ahmadinejad and the supreme leader, including an open discussion in the Majles of impeaching Ahmadinejad.<sup>306</sup>

The neoconservatives also support Iran's right to the enrichment of Uranium, but deny any military linkages (i.e., enrichment to weapons grade). "[Ahmadinejad's] government pushed ahead with its nuclear fuel enrichment program, despite new UN and U.S. sanctions between 2006 and 2010."<sup>307</sup> Most enrichment activity has occurred on the neoconservatives government watch during this period, and international negotiations to halt enrichment have similarly been rebuffed by the neoconservative government.<sup>308</sup> Neoconservative constituents among the security services also support this position, which sees a nuclear weapon as the ultimate deterrent to U.S. or coalition intervention and an end to their position of power in Iran.

#### ***b. Economic Assets and Constituents of the Neoconservatives***

The IRGC's growth from praetorian guard to becoming an economic client of the neoconservatives is rooted in the need to maintain the IRGC's military

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<sup>305</sup> Kenneth M. Pollack, *The Persian Puzzle: The Conflict between Iran and America*, 1st ed. (New York: Random House, 2004), 334.

<sup>306</sup> Katzman, *Iran Sanctions*, 45.

<sup>307</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 19.

<sup>308</sup> *Ibid.*, 79.

strength at the end of the Iran-Iraq war, while at the same time, spurring reconstruction in a resource-constrained environment.<sup>309</sup>

The Guards currently dominate most sectors of the economy, from energy to construction, telecommunication to auto making, and even banking and finance ... linked to dozens, perhaps even hundreds, of companies that appear to be private in nature but are run by IRGC veterans. So the Guards economic influence activities encompass a broad network of current and former members rather than a single official or centrally administered organization.<sup>310</sup>

Economic sanctions have only provided the neoconservatives with a convenient excuse to expand their economic interests and solidify their own patronage base at the expense of the other actors. The engineering arm of the IRGC, the Gharargah Sazandegi Khatam al-Anbia, better known by its acronym, GHORB, has been effectively privatized and now gains contracts across lucrative sectors of the economy, including the petrochemical sector, since foreign direct investment is unavailable because of sanctions.<sup>311</sup> Since winning the 2005 presidential elections, IRGC economic interests have expanded further, as their affiliated companies have “[been] awarded hundreds of no-bid government contracts in addition to billions of dollars in loans for construction, infrastructure and energy projects.”<sup>312</sup> The neoconservatives have also taken advantage of Supreme Leader Khamenei’s decision to privatize \$120 billion worth of public assets in 2005, purchasing larger stakes in formerly conservative state-controlled institutions. Purchases of privatized assets were “conducted by [IRGC] credit and finance institutions ... and their subsidiaries.”<sup>313</sup> The growth in the use of the Internet in Iran (estimated at 38 percent of the population in 2009),<sup>314</sup> has led to the growth of pro-democracy blogs and other anti-regime material on the Internet, but has also justified the security services

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<sup>309</sup> McKnight *Sanctioning Success? [Electronic Resource]: Assessing the Role of Sanctions in the Militarization of Iran*, 41.

<sup>310</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 60.

<sup>311</sup> McKnight, *Sanctioning Success? [Electronic Resource]: Assessing the Role of Sanctions in the Militarization of Iran*, 41–43.

<sup>312</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 60.

<sup>313</sup> Alfoneh, “All the Guard’s Men: Iran’s Silent Revolution,” 76.

<sup>314</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 53.

expansion into the technology sector. “In September 2009, a firm called the Mobin Trust Consortium, which was partially owned by the IRGC, bought 51 percent of shares in the Telecommunications Company of Iran ... the largest sale in the history of Iran’s stock exchange.”<sup>315</sup> This purchase was then followed by the passing of laws (using the neoconservatives’ political clout based on the IRGC) requiring all private Internet service providers (ISPs) to connect to this central hub, which gives the security services the ability to monitor all Internet activity in Iran.<sup>316</sup>

As discussed, the IRGC is also involved in illicit smuggling of goods into Iran to avoid sanctions and to line their own pockets with an estimated \$12 billion a year with the fees collected from servicing smuggling operations.<sup>317</sup> The IRGC operates a number of docks, primarily located in southern Iran, to service the smuggling fleet vis-à-vis the U.A.E. and other Gulf states.<sup>318</sup> It is also believed they have import/export sites at over 20 major airports across Iran that also contribute fees from smuggling operations.<sup>319</sup>

The neoconservatives and their security service clients have also developed their own finance networks to facilitate the purchase of public assets:

The transfers [of asset holdings] are conducted by their credit and finance institutions, such as the IRGC and Basij Cooperative foundations and their subsidiaries. The latter has its own subsidiaries ... these institutions describe themselves as noninterest or Islamic banking institutes, but they engage in everything but giving interest free loans. They function as financial arms of the IRGC and the Basij on the Tehran Stock Exchange (TSE) and elsewhere, using their leverage to purchase shares of Iranian companies.<sup>320</sup>

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<sup>315</sup> Ibid., 55.

<sup>316</sup> Ibid., 44.

<sup>317</sup> Babak Dehghanpisheh, “Smugglers for the State,” *Newsweek*, 10 July 2010, <http://www.thedailybeast.com/newsweek/2010/07/10/smugglers-for-the-state.print.html>.

<sup>318</sup> McKnight, *Sanctioning Success? [Electronic Resource]: Assessing the Role of Sanctions in the Militarization of Iran*, 46–47.

<sup>319</sup> Mehdi Khalaji, *Iran’s Revolutionary Guards Corps, Inc. Policy Watch #1273* (Washington, D.C: The Washington Institute for Near East Policy,[2007]). <http://www.washingtoninstitute.org/templateC05.php?CID=2649>.

<sup>320</sup> Alfoneh, “All the Guard’s Men: Iran’s Silent Revolution,” 76.

c. *Behavior and Motives of the Neoconservatives*

Since the 2005 election, the neoconservatives have sought to increase their control and influence in the economy, expanding their economic enterprises to become the de-facto power of the republic, while creating the conditions for a soft-coup of political power from the clerical conservatives. “Ahmadinejad rewarded the Revolutionary Guards handsomely for electing him [in 2005]. There was an immediate 74 percent increase in the development budget designed to help the Basij win government contracts.”<sup>321</sup> As they have since 2005, the neoconservatives and their security clients will continue to take advantage of the divestment of public resources and companies to build up their own holdings:

In practice, privatization of these assets has meant the Iranian leadership’s expansion from relatively transparent parts of the public sector to parts of the public sector shielded from public scrutiny, especially the IRGC and its subordinate volunteer militia, the Basij.<sup>322</sup>

Where previously there had been a distinction in Iranian politics between the ruling master clerics and their security force servants, this distinction is now blurring, to look more like a pure military dictatorship run by the security forces (specifically, the IRGC), with the clerics as figureheads. “IRGC support of Khamenei has not come cheap, and in return for its assistance against reformist groups such as the Green Movement, Khamenei has had to bribe the IRGC with political, economic, and even ideological influence.”<sup>323</sup> While remaining loyal to one cleric who appoints and approves their highest leadership<sup>324</sup>—Supreme Leader Khamenei—the neoconservatives have:

Purged the regime of its countervailing center of power in the [remaining] clergy; it has badly weakened the [Reformist] Green Movement; it has engaged civilian supporters of Khomeini in a battle for influence; and it is

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<sup>321</sup> Arjomand, *After Khomeini: Iran Under His Successors*, 152.

<sup>322</sup> Alfoneh, “All the Guard’s Men: Iran’s Silent Revolution,” 76.

<sup>323</sup> Ibid., 74.

<sup>324</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 12.

quickly transforming the Islamic Republic into a military dictatorship as Khamenei has nowhere else to look for support.<sup>325</sup>

Having won the executive branch in 2005, the neoconservatives—with more help from the IRGC in intimidating their opponents and disseminating propaganda—won control of the Majles legislature in 2008.<sup>326</sup> Their client security services also “crushed the Green Movement that emerged to protest the contested 2009 [presidential] election.”<sup>327</sup> This could not have been possible without Khamenei’s approval and support. Therefore, the neoconservatives will position themselves to be an indispensable resource to the supreme leader, while continuing their expansion in the economy (gaining further political clout) at the expense of the other actors.

### **3. Pragmatists and Their Constituents**

The pragmatists emerged as a political actor following the dissolution of the radical faction with the death of Ayatollah Khomeini in 1989. Currently, as an actor, they appear to have been effectively sidelined for the time being by the supreme leader,<sup>328</sup> and their reform agenda was similarly “overcome by events” due to the economic gains made by the IRGC in recent years (effectively ending any realistic chance for true private sector reform). This actor group’s primary benefactor and elite personality—Ali Akbar Hashemi Rafsanjani—being 77 years of age and failing in his last chance at running for President in 2005, has now been made chairman of the Expediency Council (he also resigned from the Council of Guardians in March 2011). This actor group still exists today, but their heyday was in the 1990s during Ayatollah Rafsanjani’s presidency. Members now blur between the conservative and reformist actors (mostly conservative). The pragmatists “voice the concerns of technocrats and businessmen.”<sup>329</sup> Their

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<sup>325</sup> Alfoneh, “All the Guard’s Men: Iran’s Silent Revolution,” 79.

<sup>326</sup> Arjomand, *After Khomeini: Iran Under His Successors*, 154.

<sup>327</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 19.

<sup>328</sup> Arjomand, *After Khomeini: Iran Under His Successors*, 151–152. Arjomand indicates Ahmadinejad’s 2005 victory (and Rafsanjani’s loss) was due to IRGC intervention based on instructions from the Supreme Leader.

<sup>329</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2317.

constituents, therefore, are close family and trusted associates who can participate in a client relationship (in any capacity) with their elite masters in Tehran.

Sanctions against this actor's constituency are (technically) currently in place, targeting key sectors of energy and construction, which are controlled by this actor's patrons. Partial success can be claimed with the reduction in FDI and slowing down of some investment projects. But dislodging this actor from its span of control of the political economy, or altering its behavior, will require simultaneously handing over the same levers of power and constituencies to another actor.

*a. Interests of the Pragmatists*

The pragmatists, as a group, are harder to define based on the opacity of both their membership and the business dealings that define their patronage networks. Also, their current clout in the political economy appears to have been eclipsed by the neoconservatives who emerged after Rafsanjani's terms as president ended in 1997. The pragmatist actor elites can be described as technocrats (either clerical or secular), who primarily favor reforms that support a free market to rebuild Iran's industry and economy (to include domestic and foreign investment in the private sector).<sup>330</sup> These actors also favor reforms that ease social and cultural norms, but they do not favor political reforms,<sup>331</sup> (which are distinct from the reformist actor group). They also prefer the normalization of diplomatic relations with regional neighbors and global players, downplaying the revolutionary zeal of their government, which has led to its isolation<sup>332</sup> (distinct from the conservative actor group—who still holds onto this aspect as a source of legitimacy). Some of these pragmatist elite actors, but not all, pursue reforms strictly to advance a hidden crony capitalistic agenda, irrespective of any “good sense” religious or economic reasons. “By their nature, the pragmatists [are] not overly concerned with

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<sup>330</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 16.

<sup>331</sup> Ibid., 16–17.

<sup>332</sup> Ibid., 16.



Islamic or revolutionary credentials: their whole point [is] to pursue policies that they thought best for Iran on technical grounds regardless of religious or other ideological purity.”<sup>333</sup>

It is difficult to gauge the individual intentions of the pragmatist elites on the nuclear issue, but some assessments can be drawn by words and deeds of its elite. Past statements attributed to Rafsanjani have:

Alluded to the need for Iran to be prepared for the unexpected in defense matters, and [he] most likely led the decision to hedge by seeking a weapons option ... on the nuclear issue [today], he is more likely to seek a pragmatic accommodation with the world than to accelerate enrichment.<sup>334</sup>

Perhaps, like any political actor anywhere else in the world, the pragmatist elites tepidly support the nuclear program if it helps their reelection prospects (to include not getting shut-out by the Guardian Council for opposing the program), but would be willing to negotiate internationally, once in office, to comply with Iran’s enrichment requirements per the NPT, to avoid a conflict, in opposition to the conservative and neoconservative position of no compromise. Their constituents, seeking a better business environment internationally (as well as protection domestically), would likely support this position.

***b. Economic Assets and Constituents of the Pragmatists***

The exact economic assets and constituents of this actor are hard to determine, and likely now blend in with the other actors, especially the clerical conservatives. This includes familial relationships within the bonyads, the bazaar, and some IRGC-affiliated businesses, recently purchased from government privatization efforts. Most literature focuses on the familial holdings and business dealings of Ali Akbar Hashemi Rafsanjani as the archetypical pragmatist elite actor. Upon close examination of these privatization efforts, however, Rafsanjani and his pragmatist associates, over the years, have ensured their insiders got the best deals. Their clients

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<sup>333</sup> Pollack, *The Persian Puzzle: The Conflict between Iran and America*, 242.

<sup>334</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 84.

received the best properties, contracts, and import license connections, while ensuring that billions in exchange-rate fraud benefitted the wealthiest families.<sup>335</sup> Rafsanjani's own family, "who rose from modest origins as pistachio farmers,"<sup>336</sup> became very wealthy themselves following the 1979 revolution, with relatives "operating through various foundations and front companies."<sup>337</sup> Some relatives also occupy key governmental positions in various ministries; others head various state construction and energy projects through their control of engineering companies.<sup>338</sup>

The pragmatist actors have had considerable influence over the ministry of petroleum and the NIOC since the revolution,<sup>339</sup> and their associates have been termed the "oil mafia." Access to oil rents is, therefore, critical for the Iranian political actors and is a source of contention between them, since all actors depend on it. The neoconservatives, specifically Ahmadinejad, made a bid to take control of the oil institutions after their election in 2005:

Once in power, he quickly sacked the Oil Minister but ran into problems when trying to nominate a successor. In a protracted political fight revealing the post's sensitivity, the Parliament rejected three suggested candidates before settling for a compromise.<sup>340</sup>

The neoconservatives also attempted to curb the pragmatists' hold on "banks, insurance, and state-run companies"<sup>341</sup> similarly by firing their leadership and attempting to fill replacements with neoconservative loyalists.

### *c. Behavior and Motives of the Pragmatists*

The current motives of this actor group are unclear, but they will likely continue to attempt to push through reforms based on past precedent. Rafsanjani and his

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<sup>335</sup> Klebnikov, *Millionaire Mullahs*.

<sup>336</sup> Ibid.

<sup>337</sup> Ibid.

<sup>338</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 102.

<sup>339</sup> Ibid.

<sup>340</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2318.

<sup>341</sup> Ibid.

pragmatist allies did make some legitimate attempts of economic reform during the First (1989–1993) and Second (1995–1999) Five-Year Development Plans. The party’s structural adjustment programs (SAP) introduced during Rafsanjani’s terms as president:

Included an orderly exchange-rate unification, increased fiscal and monetary disciplines, trade and business deregulation, streamlining of the state bureaucracy, privatization of money losing enterprises, and the establishment of budgetary control over the semi-independent pastoral bonyads.<sup>342</sup>

These and other reform efforts were largely frustrated by the conservatives and their clients when they infringed upon their interests. These efforts were equally botched in terms of their poor execution by the pragmatists, as well as by their own greed and favoritism of the intended recipients.<sup>343</sup>

Some literature describes these actors as “Mullahcrats,”<sup>344</sup> given their preference to provide the bulk of reform benefits to clerical insiders, their associates, and their own families.<sup>345</sup> While not all pragmatist elite actors are corrupt—it could be said that as a rule of thumb they seem to push for reforms that will bring about private sector reform that will strengthen the Iranian economy—but oppose reforms that will alter the political balance that exists in government. They are less concerned with reforms based entirely on religious morality, and desire to see an “easing of social and cultural controls.”<sup>346</sup> Some corrupt elements are concerned with simply increasing their own wealth and the strength of their patronage networks via reforms and privatization, but their distinction from the conservative actor group is difficult to discern.

#### **4. Reformists and Their Constituents**

The roots of the reformist actors (and the green movement) can be traced to the clerical works of the dissident Shia cleric Grand Ayatollah Ali Montazeri and the

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<sup>342</sup> Amuzegar, *Iran’s Economy and the US Sanctions*, 189.

<sup>343</sup> Ibid.

<sup>344</sup> Klebnikov, *Millionaire Mullahs*.

<sup>345</sup> Ibid.

<sup>346</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 16.

sociological works of Ali Shariati.<sup>347</sup> Montazeri, who assisted drafting the original revolutionary constitution, and originally a radical himself, eventually took a different view of the absolute powers of the supreme leader—believing the “[Supreme Leader] office holder was meant to arbitrate and guide ... whose function was to manage the [political] system and restore balance when necessary.”<sup>348</sup> This view conflicted with the conservatives, who ultimately dismissed him as Khomeini’s heir apparent in 1989, but his later works from Qom, criticizing the revolutionary government, inspired future reformists.<sup>349</sup> The reformist label eventually became “a new name for the old-time radical faction, which had gone through an ideological transformation and rethought its political creed.”<sup>350</sup> Montazeri’s death in December 2009, coinciding with the green movement protests, sparked further massive demonstrations.<sup>351</sup>

The reformists formally emerged in 1997 with the election of President Khatami. The reformists are the weakest of the four actors in the Iranian political economy, but present the best hope for change given their record of the advancement of peaceful dialogue and level of worldwide support. The recent green movement is associated with this political actor as it has “embodied the frustrated aspirations of Iran’s century-old quest for democracy and desire for peaceful change.”<sup>352</sup> Its current leaders are Mir Hossein Mousavi, the loser of the 2009 presidential elections, his activist wife, Zahra Rahnavard, reformist politician, Mehdi Karroubi, and former president, Khatami.<sup>353</sup> Many other activists and leaders exist, hundreds of which were put on televised trials in the fall of 2009 and forced to confess that “the Green Movement was a creation of the United States and its goal was to weaken the Islamic Regime.”<sup>354</sup>

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<sup>347</sup> Seifzadeh, *The Landscape of Factional Politics and its Future in Iran*, 62.

<sup>348</sup> Ali M. Ansari, *Confronting Iran : The Failure of American Foreign Policy and the Next Great Crisis in the Middle East* (New York: Basic Books, 2007), 120.

<sup>349</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 43.

<sup>350</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2316.

<sup>351</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 43.

<sup>352</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 41.

<sup>353</sup> Ibid.

<sup>354</sup> Ibid., 43.

Broadly speaking, the Reformist's clients are students and lay intellectuals<sup>355</sup> and also include a few left-leaning clerics based out of academic institutions.<sup>356</sup> Support for this group is often issue dependent. "The social basis of this group is vast and diverse... generally, as part of the modern sector of society, eighteen different political parties represent the reformist's social base."<sup>357</sup> Prior to the 2004 Majles elections, the reformists were the dominant party in the legislature, but have lost ground to the neoconservatives.

Economic sanctions, as they exist now, are not benefiting the reformist actor groups. "Smart sanctions focused on weakening the regime's ideological and oppressive apparatus can facilitate the maturation of this [reformist] movement. A military assault could sideline or kill the movement for the foreseeable future."<sup>358</sup> While sanctions do reduce the overall amount of available rents to other actors, the reformist groups are not the beneficiaries. The overall effect of sanctions is to reduce the size of the overall "economic pie" of Iran, but the reformist slice has not gotten bigger as a percentage of the whole because of them. Specific CISADA sanctions provisions to strengthen the opposition exist and partners have imposed similar sanctions, but their effect on the political economy is negligible. Details on specific sanctions will be presented in the next chapter, but specific to sanctions passed in legislation by the U.S. Congress [not authorized funding of reformist actors to promote democratic change via black operations] to support democratic change or alter Iranian Foreign Policy exist, but are largely symbolic in value. These include sanctions "to support the opposition's ability to communicate, to reduce the regime's ability to monitor and censor Internet communications and to identify and sanction Iranian human rights abusers."<sup>359</sup>

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<sup>355</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2317.

<sup>356</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 36.

<sup>357</sup> Seifzadeh, *The Landscape of Factional Politics and its Future in Iran*, 62.

<sup>358</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 44.

<sup>359</sup> Katzman, *Iran Sanctions*, 32.

*a. Interests of the Reformists*

The reformists' interests, at least among the elites, are better foreign relations with nations who mutually respect Iranian interests<sup>360</sup> and an economic, cultural, and political liberalization to include: an independent judiciary; curtailing the security services role in the economy; full parliamentary oversight of all appendages of government, and limits on the supreme leader's extra-constitutional power.<sup>361</sup> "Reformists are specifically concerned with the removal of restrictions on socio-cultural aspects of human life. A reformist interpretation of the constitution forbids the government from interfering in the private life of the populace."<sup>362</sup>

Unlike the other actor groups, the reformist elites believe real reform must include domestic political reform in society, which will create a better business environment for domestic and foreign investment. "Reformists ... believe political reforms are necessary to set the preconditions for reforms in all other spheres of life and in economics, in particular. As a result, they believe the root cause of economic downturns is the insecurity to invest."<sup>363</sup>

Regarding the nuclear issue, the reformists are believed to be the best group who would legitimately negotiate over the issue, which would not include giving up Iran's right to peaceful enrichment. Discussing the nuclear issue, green movement leader and former reformist candidate, Mir Hossein Mousavi, "has suggested a

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<sup>360</sup> Pollack, *The Persian Puzzle : The Conflict between Iran and America*, 310.

<sup>361</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 18.

<sup>362</sup> Seifzadeh, *The Landscape of Factional Politics and its Future in Iran*, 68.

<sup>363</sup> Ibid., 67.

reasonable accommodation with the international community,”<sup>364</sup> which can be interpreted to mean a willingness to work within the NPT to reach an ending to the crisis. However, internal politics and the reformists’ desire to simply survive, politically, have gotten in the way. Discussions of an Iranian fuel enrichment swap for Tehran’s reactor, hammered out in Geneva in October 2009, was initially accepted by Ahmadinejad’s government:

But the reactor deal was soon criticized by Iran’s new Green Movement opposition, as well as conservatives in the regime, largely for political reasons. Ahmadinejad’s opponents did not want the president to get credit for any agreement favorable to Iran. Some leaders also may have feared that any change in the Islamic-Republic’s underlying anti-Americanism would threaten the existence of their system.<sup>365</sup>

Among their constituents, of whom the educated youth is the largest client, the reforms desired are more economic in nature. Discontent with poor employment opportunities, as well as achieving more social and political freedoms, constitute their chief concerns. Support for negotiation on the nuclear issue can be found among the clients of the reformists—the educated youth and intelligentsia who see peaceful Uranium enrichment as a right, but largely do not support enrichment to weapons grade.

***b. Economic Assets and Constituents of the Reformists***

Being that the clients of the reformists are primarily students and intellectuals, their economic base is decidedly slim. These clients “lack access to the parallel power centers and “shadow” economic forces like the religious foundations and the Revolutionary Guard.”<sup>366</sup> However, like the pragmatists, the reformists have “built extensive ties with private entrepreneurs during their years of formal control of the state apparatuses under Khatami’s Presidency.”<sup>367</sup> These exact ties are not clear, but it is likely

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<sup>364</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 85.

<sup>365</sup> Ibid., 147.

<sup>366</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2318.

<sup>367</sup> Ibid.

that they overlap in some degree with the pragmatist actor group who desire to see the conditions set for a better business environment:

An indication of the strength of these links came with Ahmadinejad's cold-shouldering of the business elite after his 2005 rise to power. The neoconservative president made thinly veiled accusations that leading private investors had made their wealth as protégé's of pragmatic conservatives and reformists, and said that he would allocate resources to small-scale enterprises instead of big actors.<sup>368</sup>

The youth are now considered clients of the reformists for several reasons, mostly because of demonstrated action versus stated ideology, which has shifted to support differing candidates at different times. While it is true that pro-regime youth organizations exist in Iran, such as those associated with the Basij, the group is not monolithic and the majority of the youth in Iran desire political and social freedoms that happen to coincide with the reformists' interests. Iran's first organized student movements' agendas have evolved over the last three decades:

From a focus on Islamic ideology to individual rights under Islamic rule. The group's calls for political and social openings contributed to the reform movement's birth in the late 1990s. Members were involved in the 1999 student protests, [which were] the largest demonstrations until the 2009 elections."<sup>369</sup>

The youth constitute the largest bloc in the green movement and, as a constituency, faced the largest share of the conservatives and neoconservatives' crack-down over it.<sup>370</sup>

The youth constitute 40 percent of the electorate and this percentage is slowly rising.<sup>371</sup>

Youth is the largest population block in Iran. Over 60 percent of Iran's 73 million people are under 30 years old... Iranian youth are among the most politically active in the 57 nations of the Islamic world. As the most

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<sup>368</sup> Ibid.

<sup>369</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 51.

<sup>370</sup> Ibid., 50.

<sup>371</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 49.



restive segment of Iranian society, the young also represent one of the greatest long-term threats to the current theocratic rule.<sup>372</sup>

What the youth have in numbers and potential votes, they lack in economic wealth:

The government generates only about 300,000 of the roughly 1 million jobs needed annually to absorb young people entering the labor market... unemployment among youth has almost doubled since 1990. Young people between 15 and 29 make up 35 percent of the population but account for 70 percent of the unemployed.<sup>373</sup>

It is important to note that the reformist actor group does not necessarily resonate with the working and lower-middle classes. These demographics largely still remain the clients of their neoconservative patrons who have steered resources in their direction at the expense of the bigger private sector actors.<sup>374</sup> Ahmadinejad has campaigned on a populist platform to distribute patronage and largesse to these constituencies in the name of social justice<sup>375</sup> and has cut general subsidies and used the savings to direct cash handouts to these demographics instead, which have actually hurt this demographic due to the rise in inflation.<sup>376</sup> Campaigns of free market reforms have simply failed to capture the hearts of these demographics, which prefer the candidate who promises social justice against the ruling clerical elite and their visible wealth.

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<sup>372</sup> Ibid.

<sup>373</sup> Ibid.

<sup>374</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2318.

<sup>375</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 18.

<sup>376</sup> Ibid., 105.

“Ahmadinejad’s populist message of economic equality won over the promises of neoliberal economic projects espoused by other candidates, even those running under the conservative banner.”<sup>377</sup>

**c. *Behavior and Motives of the Reformists***

The reformist elites desire political, social, and economic change to benefit Iranians and have organized and led peaceful protests to do so. However, so far they have refused to operate outside the constitution or the law to achieve their objectives. This is one of their greatest weaknesses, as no reformist leader can be found for the reformist constituencies to galvanize behind to achieve their goals. Leaders who exhibit any of these qualities are quickly eliminated by the regime anyway, usually through arbitrary arrests and lengthy jail sentences. President Khatami’s failure to respond to friendly diplomatic overtures from the West during the Clinton administration, and support the violent student protests that broke out across Iran during the summer of 1999, was an early indicator of the limits of the reformist elites. “The hard liners had digested the lesson from the [1999] summer that Khatami would not lead a revolution and would back down when faced with a choice between doing so or giving in. That gave them the upper hand, and they used it.”<sup>378</sup> More recently, Mir Hossein Mousavi’s “unwillingness to criticize Khamenei and his insistence on working within the constitution convinced some Iranians that he no longer reflected the [Green] movements’ views.”<sup>379</sup>

As stated, the youth now constitute the greatest constituency client of the reformist elites and they represent the greatest threat for a velvet revolution to the regime.

By 1997, their growing numbers helped elect reformist President Mohammad Khatami. But as he failed to produce change, the young pulled back. The partial youth boycott of the 2005 presidential election

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<sup>377</sup> Monshipouri and Assareh, “The Islamic Republic and the “Green Movement”: Coming Full Circle,” *Middle East Policy* 16, no. 4 (Winter 2009), 3.

<sup>378</sup> Pollack, *The Persian Puzzle: The Conflict between Iran and America*, 337.

<sup>379</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 43.

was key to Mahmoud Ahmadinejad's election. Their reentry into politics into politics in the 2009 election seriously altered Iranian politics.<sup>380</sup>

By 2009 they were more willing to take matters into their own hands and defy the conservative and neoconservative leadership. "Many Iranian youth have for a long time felt alienated from the Islamic Republic, and recent electoral fraud has decreased their faith in change through democratic means. Yet the [reformist] movement is still largely nonviolent."<sup>381</sup> Use of the Internet and blogs to air grievances has now become the primary method to air grievances against the regime, which the youth lead.<sup>382</sup> "Iran is one of the most tech-savvy societies in the developing world, with an estimated 28 million Internet users, [which is] led by youth... Iran boasts between 60,000 and 110,000 active blogs, one of the highest numbers in the Middle East, led by youth."<sup>383</sup>

## **B. SOURCES OF RENTS AND COMPETITION BETWEEN THE ACTORS**

It is important to note that petrochemical exports play a significant part in the Iranian political economy and have played a significant role in shaping the political system. Iran is a founding member of OPEC and is now that organization's second largest producer and exporter of crude oil, after Saudi Arabia.<sup>384</sup> Iran is also the fifth largest global producer of oil (5.3 percent world market share in 2009)<sup>385</sup> and the second largest producer of natural gas<sup>386</sup> (4.4 percent of world market share in 2009).<sup>387</sup> Iran has

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<sup>380</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 49.

<sup>381</sup> Monshipouri and Assareh, *The Islamic Republic and the "Green Movement": Coming Full Circle*, 9.

<sup>382</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 54.

<sup>383</sup> *Ibid.*, 52.

<sup>384</sup> Anonymous, "Iran Energy Data, Statistics and Analysis - Oil, Gas, Electricity, and Coal," U.S. Energy Information Administration - U.S. Department of Energy, <http://www.eia.gov/countries/cab.cfm?fips=IR> (accessed 14 October, 2011).

<sup>385</sup> Anonymous, *BP Statistical Review of World Energy June 2010* (London, U.K.: BP Statistical Review of World Energy [2011]).

<sup>386</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 101–102.

<sup>387</sup> Anonymous, *BP Statistical Review of World Energy June 2010*, 24.

about 10 percent of the world's total oil reserves,<sup>388</sup> the third-largest in the world<sup>389</sup> — and about 15.8 percent of the world's total natural gas reserves,<sup>390</sup> the second largest in the world.<sup>391</sup> The Iranian Ministry of Petroleum controls the NIOC, which has struggled to keep up production at 3.5 million BPD.<sup>392</sup>

Access to oil is, therefore, critical for the Iranian government and this sector of the economy remains a target for sanctions, since all actors depend on it for maintaining its control of the state. “Iran’s petroleum sector generates about 20 percent of Iran’s GDP (which is about \$870 billion), 80 percent of its exports, and 70 percent of its government revenues.<sup>393</sup> Yet, tracking the exact intra-governmental allocation of government spending is difficult,<sup>394</sup> and information on IRGC and IRGC-affiliated black-market contributions is impossible.<sup>395</sup> This is by design, as this allocation is intentionally opaque.

Whatever actor can gain control of state offices can control the allocation of oil rents for patronage and thus further their control of the economy. Bribery and favor-seeking is also a part of Persian culture and brings new clients for the actor. “Competition for positions in the Mayor’s office and similar jobs is fierce. Similarly, firms spend resources to court bureaucrats in order to obtain privileges and favors.”<sup>396</sup> These actors either control the rents directly or put pressure on the regulatory or bureaucratic bodies that allocate funds to preferred parties.<sup>397</sup> “The most important channels for distributing

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<sup>388</sup> Anonymous, *Iran Energy Data, Statistics and Analysis - Oil, Gas, Electricity, and Coal*, 2.

<sup>389</sup> Ibid.

<sup>390</sup> Anonymous, *BP Statistical Review of World Energy June 2010*, 22.

<sup>391</sup> Anonymous, *Iran Energy Data, Statistics and Analysis - Oil, Gas, Electricity, and Coal*, 8.

<sup>392</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 100.

<sup>393</sup> Katzman, *Iran Sanctions*, 1.

<sup>394</sup> Green et al., *Understanding Iran*, 17.

<sup>395</sup> Ibid., 20–21.

<sup>396</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2319.

<sup>397</sup> Ibid., 2318.

oil rents are development projects and subsidized loans.”<sup>398</sup> In the past, subsidized energy had also served the actors in providing patronage to their clients.

## **1. Development Projects**

Development projects, steered by the actors to their favored clients and/or contractors, are a major way the actors distribute patronage. Often, these are given directly in the form of no-bid contracts.

One way to create rents from development projects such as dams, roads, and hospitals is for the bureaucrats running the project to make a generous estimation of the projects costs. The difference between the official cost of the project and the actual cost may then be split between the contractor and the bureaucrats.<sup>399</sup>

Many of these types of no-bid contracts have been awarded to the IRGC’s engineering arm, GHORB, an entity that remains sanctioned under U.S. executive order 13382, also coincident with sanctions under UN Resolution 1929<sup>400</sup> (Katzman and Library of Congress; Congressional Research Service 2011). Other firms that engage in this activity also remain sanctioned.

## **2. Subsidized Loans**

Cheap credit is another means of distributing patronage. Access to this credit is preferential and based upon the client’s connections to the actor who can influence the state banks. Money is often used for purposes other than intended and sometimes not repaid without any consequences.<sup>401</sup> As has been observed, the conservatives have the most influence on the control of nationalized banks, with the neoconservatives slowly developing their own parallel banking and finance capabilities. It is unclear where these two capabilities overlap, but both actors still use subsidized loans to their favored clients as a form of patronage to further their own political influence.

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<sup>398</sup> Ibid.

<sup>399</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2318.

<sup>400</sup> Katzman, *Iran Sanctions*, 60–62.

<sup>401</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2318.

The Iranian government has direct control over lending and investment activities of commercial banks... in addition, most of the financial intermediaries loan portfolios are comprised of low-return loans to state-owned enterprises and quasi-government agencies, such as the bonyads. By IMF estimates, nonperforming loans have amounted to more than one-fifth of Iranian banks loan portfolios... in economic sectors in which the Iranian government is involved in directed lending.<sup>402</sup>

### **3. Cash Transfers to Client Constituencies**

General subsidies are scheduled to be phased out by 2015, following an agreement reached between the factions in 2010.<sup>403</sup> Repeal of these subsidies was difficult but necessary—as their costs had risen to approximately \$83.75 billion or 25 percent of GDP in 2009. In the new arrangement, the savings from subsidies will be used as a new form of cash payments to targeted constituencies:

50 percent for direct cash payments to people who qualify for aid; 30 percent to industries that rely heavily on subsidies, and to improve they energy sector and public transportation, and; 20 percent directly to the Treasury to cover government costs of implementation and reduce dependence on oil revenues.<sup>404</sup>

Ahmadinejad initially resisted parliamentary oversight of the distribution of these funds, naturally, as they can be manipulated into a form of patronage, but in the final arrangement, the parliament will have audit authority.<sup>405</sup>

The weakness of distributing cash in lieu of subsidies to the poorest of Iranian society, as well as select industries, has been the massive rise in inflation. Inflation has increased with these cash handouts to approximately 30 percent in 2008,<sup>406</sup> ultimately weakening the very constituency (the poor) targeted for assistance by weakening their purchasing power. “Ahmadinejad’s profligate spending also drained the Treasury of

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<sup>402</sup> Shayerah Ilias, *Iran’s Economic Conditions: U.S. Policy Issues* (Washington, D.C.: Congressional Research Service, [2010]), 15.

<sup>403</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 104.

<sup>404</sup> Ibid., 105.

<sup>405</sup> Ibid., 106.

<sup>406</sup> Ibid., 105.

billions from oil revenues, while contributing little to improve Iran's aged and ailing infrastructure."<sup>407</sup> Inflation also theoretically makes it difficult to ensure payments to the security services that are the neoconservative client constituents, but as in all authoritarian states, the security services would receive a priority (as a pillar of the regime) to see their pay keep parity with inflation.

#### **4. Monopolies and Tariffs**

Monopolies on the imports and distribution of consumer goods such as rice, tea, sugar, and tobacco exist in Iran. Held by the bonyads, they are tolerated by the government, even if not officially sanctioned.<sup>408</sup> This can be considered a regulatory rent,<sup>409</sup> especially to the conservative actors who remain in control of the bonyads. United States' sanctions, while banning imports and exports from Iran, maintain an exemption for food products.<sup>410</sup>

### **C. IRANIAN ACTORS' VULNERABILITIES**

Each actor's patron and client relationships have been examined, as have the sources of rents each depends on. This section briefly turns to the sources of competition and potential weaknesses, between each actor, to identify possible areas for exploitation by smart sanctions.

#### **1. Infighting between Conservatives and Neoconservatives**

The ascendancy of the neoconservatives in Iranian society, both politically and economically, is a sign that the broader elite clerical base has lost popular support.

Mahmoud Ahmadinejad's victory was equivalent to another revolution within the Islamic Republic, one in which a new generation of hardliners were keen on returning Iran to the fundamentals of the 1979 Islamic Revolution, when the dispossessed and underprivileged were given hope

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<sup>407</sup> Ibid.

<sup>408</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2319.

<sup>409</sup> Ibid.

<sup>410</sup> Katzman, *Iran Sanctions*, 41.

for a better life. Ahmadinejad argued that the revolution had gone awry, privileging clerical rulers who had become far removed from the struggles of average Iranians suffering from double-digit unemployment rates and rampant inflation.<sup>411</sup>

There are splits between the conservatives and neoconservatives, mostly over control of appointments to key positions in government, which have led to the apparent loss of support from the supreme leader for president, Ahmadinejad. This split has also widened between conservatives and neoconservatives in the parliament “to the point at which there has been open discussion in Iran’s parliament since June 2011 on impeaching Ahmadinejad.”<sup>412</sup> International sanctions, or differences in economic or foreign policy, do not appear to be the cause of the split<sup>413</sup> but rather the neoconservatives push for greater control of the institutions of government. Ahmadinejad’s attempts to assert greater control over government institutions like banks, insurance and state-run companies by replacing their leadership with his own neoconservative associates, is met with resistance in the Majles and are a sign of the conflict between the two actors as positions of power and control of rents are contested.<sup>414</sup>

Ahmadinejad’s (i.e., the neoconservative’s) attempts to control the distribution of cash payments without parliamentary oversight is a recent indication of his attempts to outmaneuver the conservative clerics to solidify his client constituency among the poor, some of whom still hold nostalgia for the clerical revolution and its promise of religious leadership. Despite this example ending in an apparent draw, other examples of Ahmadinejad and the neoconservatives attempting to assert greater influence include: “Expanding credit [to favored clients] and spending in a freewheel fashion; Feuding openly with a series of cabinet ministers and Central Bank chiefs; Dismantling the [economic] planning bureaucracy, and; Disempowering government technocrats.”<sup>415</sup> These efforts have done more than raise eyebrows among the conservatives, as most are

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<sup>411</sup> Monshipouri and Assareh, *The Islamic Republic and the “Green Movement”: Coming Full Circle*, 3.

<sup>412</sup> Katzman, *Iran Sanctions*, 45.

<sup>413</sup> Ibid.

<sup>414</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2318.

<sup>415</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 98.



designed to weaken their economic and constituent base. Despite these efforts, the conservatives (via the supreme leader), still hold the upper hand by controlling the nonelected organs of state power that can overturn legislation and neoconservative government appointments. The neoconservatives are mitigating this by showcasing these efforts in a populist manner—social justice—to appeal to overlapping constituencies such as the poor and the security services.

## **2. Corruption of the Pragmatists**

The pragmatists are viewed by the international audience as being an actor with a ray of hope in an otherwise intractable sea of conservative ideologues, but the shifting of loyalties in Iranian politics makes it difficult to determine who is a pragmatist and who is a conservative.<sup>416</sup> It is true that during Rafsanjani's presidency there were efforts at international rapprochement, as Iran resumed diplomatic relations with Saudi Arabia, Morocco, and Egypt and he also helped obtain the freedom of American hostages held by Lebanese hezbollah.<sup>417</sup> The easing of social and cultural restrictions was also seen as a sign of a new era in Iran, as was the invitation for outside FDI in Iran's economy. More recently, Rafsanjani and other former pragmatist politicians have called for "more tact and management" regarding the conservatives and neoconservatives' hard-line handling of Iranian international affairs, specifically regarding the plot to kill the Saudi Ambassador to Washington in October 2011.<sup>418</sup>

But the clerics are domestically viewed as corrupt themselves, and despite some pragmatist leanings, as a group, they likely would not advance the kind of liberal reforms needed to alter governmental policy on the nuclear issue should sanctions somehow weaken their competitors. Their vested interests in the economy would also not generate true private sector growth to take power out of the conservatives' and neoconservatives'

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<sup>416</sup> Peter Jones, "Succession and the Supreme Leader in Iran," *Survival* 53, no. 6 (2 December 2011), 115.

<sup>417</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 16.

<sup>418</sup> Thomas Erdbrink, "In Iran, a New Challenge to Hard-Liners," *The Washington Post* (20 October 2011). [http://www.washingtonpost.com/world/middle\\_east/in-iran-a-new-challenge-to-hardliners/2011/10/19/gIQA3YWN1L\\_story.html](http://www.washingtonpost.com/world/middle_east/in-iran-a-new-challenge-to-hardliners/2011/10/19/gIQA3YWN1L_story.html).

hands. With the average Iranian income at \$10,600 per capita a year in 2010,<sup>419</sup> stories of Rafsanjani's and other mullah's considerable wealth have been around for a long time.

The gossip on the street, going well beyond the observable facts, has the Rafsanjani's stashing billions of dollars in bank accounts in Switzerland and Luxembourg; controlling huge swaths of waterfront in Iran's free economic zones on the Persian Gulf; and owning whole vacation resorts on the idyllic beaches of Dubai, Goa, and Thailand.<sup>420</sup>

Journalistic inquiries into Rafsanjani's dealings have led to lengthy prison sentences, mutilations and death.<sup>421</sup>

Since the revolution, this actor group has also had considerable influence over the ministry of petroleum and the NIOC,<sup>422</sup> and their associates have been termed the "oil mafia." The neoconservatives, specifically Ahmadinejad, made a bid to take control of the oil institutions after their election in 2005. "Once in power, he quickly sacked the Oil Minister but ran into problems when trying to nominate a successor. In a protracted political fight revealing the post's sensitivity, the Parliament rejected three suggested candidates before settling for a compromise."<sup>423</sup> The neoconservatives also attempted to curb the pragmatists' hold on "banks, insurance, and state-run companies"<sup>424</sup> in a similar manner, by firing their leadership and attempting to fill replacements with neoconservative loyalists.<sup>425</sup>

### **3. Weakness of the Reformists**

The reformists face a difficult challenge due to the weakness of their primary constituencies—the students and intellectuals in Iranian society who have little to no economic wealth to draw from. There are indications that some clerics have also become

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<sup>419</sup> "CIA World Factbook - Iran," United States Central Intelligence Agency, <https://www.cia.gov/library/publications/the-world-factbook/geos/ir.html> (accessed 24 October 2011).

<sup>420</sup> Klebnikov, *Millionaire Mullahs*.

<sup>421</sup> Ibid.

<sup>422</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 102.

<sup>423</sup> Bjorvatn and Selvik, *Destructive Competition: Factionalism and Rent-Seeking in Iran*, 2318.

<sup>424</sup> Ibid., 2318.

<sup>425</sup> Ibid.

more left-leaning, but these individuals, as has been shown, are mostly associated with academia and also lack an economic wealth base. This is obviously due to the conservatives' and neoconservatives' control of the political economy and the absence of an open, free market economy. But what this group lacks in economic power, it makes up for in sheer numbers and technical savvy. As has been shown, the youth constitute about 40 percent of the population but suffer from 70 percent unemployment.<sup>426</sup> The economic frustration of the youth was translated into the green movement, which "reached its height when up to 3 million peaceful demonstrators turned out on Tehran streets."<sup>427</sup>

Despite the youth's use of the Internet to air its grievances, the regime is able to monitor and censor its use. "The regimes technical filtering and censorship of the internet is one of the most extensive in the world."<sup>428</sup> The conservatives have passed legislation requiring all Internet Service Providers (ISP's) to utilize filtering systems, block unauthorized sites, and connect through the state-owned telecommunications company, which is now controlled by the IRGC.<sup>429</sup> The IRGC also established its own Cyber Defense Command in 2009 and monitors internet activity.<sup>430</sup> United States' economic sanctions have been put in place to assist these activists, which will be discussed in the next chapter, but the effects of these efforts are questionable.

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<sup>426</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 49.

<sup>427</sup> Ibid., 41.

<sup>428</sup> Ibid., 54.

<sup>429</sup> Ibid., 54–55.

<sup>430</sup> Ibid., 55.

## D. CONCLUSION

This chapter has examined the political actors in Iran and their constituents, as well as their sources of rent competition and their potential vulnerabilities. Two broad conclusions can be drawn from this analysis regarding the best way to alter Iranian behavior and policies via economic sanctions: sanctions should focus on weakening the conservative and neoconservative actors due to their infighting over political control, rents, and overlapping constituencies and clients and, sanctions should focus on supporting the youth, which are largely the clients of the reformists who offer the best hope of bringing about change in Iran. As has been shown during the 2009 green movement, the youth's numbers and significant economic grievances have already changed the political landscape of Iran. Given that the pragmatist actors have largely blended into other actor groups and can now be regarded as nonactive players—sanctions should focus on the three remaining actors.

Smarter sanctions should aim to accomplish these objectives simultaneously for the best chance of success. Sanctions, as they exist today, primarily seek to weaken the conservative and neoconservative actors and are having some success in limiting the amounts of long-term rents available to them and their clients. They have also complicated Iran's business environment, both domestically and internationally.<sup>431</sup> However, these sanctions are also, arguably, increasing these actors' control of the political economy—as the IRGC and other quasi-state actors have moved in to fill economic voids left by other departing foreign and domestic investors. These sanctions gains have also not translated into increased rents or political clout for the reformist actors or their youth constituents, nor have they broadened support for the reformist actors among other constituencies. “Some argue that difficult economic sanctions are contributing to the political quiescence of Iranian labor because the working class fears loss of pay from participation in demonstrations or from regime retaliation.”<sup>432</sup>

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<sup>431</sup> Ilias, *Iran's Economic Conditions: U.S. Policy Issues*, 34.

<sup>432</sup> Ibid.

Perhaps the best way to envision the Iranian political economy is as a pie, cut up into four different pieces. The conservatives and the neoconservatives currently have the largest slices of the pie—arguably three-fourths of it. The pragmatist actors, as has been shown, have largely disappeared as a coherent actor and have crumbled into the conservative piece. The size of the pieces ensures domination of both politics and the economy and allows the conservatives and neoconservatives to dictate the Iranian policy the U.S. seeks to change. The reformists have the other slice—the smallest piece. As the weakest actor, they have little say in the political economy and are more of a nuisance to the other actors. Sanctions, as they exist today, are shrinking the size of the entire pie, but not changing the makeup of the size of the slices. Smart sanctions, therefore, should exploit the seams of the slices, and somehow grow the size of the slice of the reformist slice while shrinking the size of the other pieces. How to do this, exactly, is the subject of the next chapter.

#### IV. ALTERING IRANIAN SANCTIONS

As has been shown in Chapter II, economic sanctions regimes have the best chance of achieving their goals when the actors in the political economy face political competition brought about by an independent economic base of wealth. The Iranian conservative and neoconservative actors and their client constituents control most of the economic and political activity in the Iranian political economy. The current Iranian economic sanctions regime is designed to alter Iranian policies on a number of fronts, with the most recent U.S. and UN resolutions and sanctions targeting organizations and individuals linked to “involvement in Iran’s nuclear and ballistic missile programs, or affiliated with the IRGC”<sup>433</sup> (which are associated with the conservative and neoconservative actors). The Iranian nuclear issue is at the forefront of policies the international community is concerned about.

The reformist actor elite, if they could achieve power, offer the best hope of the Iranian leadership achieving the desired political goals of the economic sanctions currently in place—ultimately, an Iran that abides by international norms and behaviors (i.e., becomes a status-quo state). The conservative and neoconservative actors continue to resist this change, hanging onto their revolutionary ideals as a source of legitimacy, while insulating themselves with further entrenchment in the economy, solidifying political control. This control of the political economy has allowed them to emasculate the reformist actors, denying them access to economic wealth—and the chance to gain a sustained political presence. A sustained political presence would allow for the growth of popular support, which would lead to changes in institutions that insulate the conservatives and neoconservatives from political and economic threats.

The goals of economic sanctions should therefore be to grow the strength of the reformist actors (and their clients) economically, so their political clout can grow as well. A brief review of existing Iranian sanctions and their general inadequacies has been provided in Chapter II. Rather than recount the extensive listing of economic sanctions

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<sup>433</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 122.

against Iran, this chapter will review the effects of current economic sanctions on the Iranian political economy. Special attention will be given to examination of the differences between the real and intended effects of these sanctions on the political economy and the actors within it. External factors, such as the oil shield and weak sanctions enforcement will also be examined as an insulating factor to the economic sanctions regime. Finally, recommendations for adjustments in the Iranian sanctions policy will be made.

Although mentioned in Chapter II, it is worth mentioning again that “there is no agreement among U.S. officials on the specific objectives of [U.S.] sanctions on Iran, which makes it hard to judge how successful they have been.”<sup>434</sup> UN sanctions, while specific in application and more narrow in focus, are equally difficult to ascertain effectiveness in both their economic and political effects.

Since 2006, the UN Security Council has passed six resolutions critical of Iran for its controversial nuclear program. Each resolution was designed to increase pressure on Tehran to suspend its Uranium enrichment and ballistic missile development programs, two of three critical steps in obtaining a nuclear weapons capability.<sup>435</sup>

#### **A. EFFECTS OF CURRENT SANCTIONS ON THE IRANIAN POLITICAL ECONOMY**

The current economic sanctions against Iran are designed to impact three broad categories, of which the ultimate effects are difficult to determine due to the subjective nature of the analysis,<sup>436</sup> as well as “disagreements over what sanctions are meant to achieve.”<sup>437</sup> U.S. and UN sanctions are broadly designed to: slow investment in Iran’s petroleum sector, thus decreasing rents to the Iranian economy for other activities; deny Iranian (and associated) persons and institutions involved in proliferation and terrorist

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<sup>434</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 118.

<sup>435</sup> Ibid., 119.

<sup>436</sup> Anonymous, *Iran Sanctions: Impact in Furthering U.S. Objectives is Unclear and should be Reviewed* United States Government Accountability Office, [2007].

<sup>437</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 116.

activities access to the international banking system and; provide a forum of legitimate international concern for Iranian policies, specifically its nuclear policies.<sup>438</sup>

Official net assessments of U.S. and UN sanctions impacts on the Iranian economy (and their effects on the political actors) do not exist<sup>439</sup> or are only available in a classified format. What sanctions information U.S. agencies do collect (typically only on the areas they are responsible to enforce) is uncoordinated and disparate and not collated into a final assessment of sanctions effects.<sup>440</sup> “Except for Treasury, the agencies do not collect data demonstrating the direct results of their sanctioning and enforcement actions, such as the types of goods seized under the trade ban or the subsequent actions of sanctioned entities.”<sup>441</sup> Per the CISADA act of 2010, the administration is required to “investigate reports of certain sanctionable activity where credible evidence is received and make a determination in writing to Congress whether such activity has indeed occurred. The President would then be expected to impose or waive sanctions.”<sup>442</sup> Given the expansion of sanctions in the 2010 CISADA legislation specifically targeting refined petroleum, the Government Accountability Office (GAO) continues to recommend the administration establish a baseline of sanctions impacts and conduct an overall net assessment of sanctions effects.<sup>443</sup>

One aspect of international sanctions remains clear: international economic sanctions have not altered Iran’s nuclear enrichment policy and have not applied sufficient pressure to induce Iran to negotiate a compromise that would limit their nuclear development.<sup>444</sup> Sanctions do not appear to be altering Iran’s other policies either, such

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<sup>438</sup> Anonymous, *Iran Sanctions: Impact in Furthering U.S. Objectives is Unclear and should be Reviewed*, 3.

<sup>439</sup> Ibid.

<sup>440</sup> Joseph A. Christoff, *Firms Reported to have Commercial Activity in the Iranian Energy Sector and U.S. Government Contracts* (Washington, DC: U.S. Govt. Accountability Office, 2010), 8.

<sup>441</sup> Anonymous, *Iran Sanctions: Impact in Furthering U.S. Objectives is Unclear and Should Be Reviewed*, 3.

<sup>442</sup> Joseph A. Christoff, *Iran Sanctions: New Act Underscores Importance of Comprehensive Assessment of Sanctions’ Effectiveness*, U.S. Government Accountability Office, [2010]).

<sup>443</sup> Ibid.

<sup>444</sup> Katzman, *Iran Sanctions*, 44.



as support for terrorism and human rights abuses. It can only be reasoned that sanctions are not altering the internal balance of power in Iran (in the short term) to promote opposition groups who offer the best hope of aligning Iranian policy to sanctions objectives (i.e., reformists). However, the recent intensification of conflict among the conservative and neoconservative factions, that played out over 2011, fragmented the elite power structure, indicates a concern among the elites of the anticipated long-term effects of sanctions and reduction of rents. Specifically, the struggle “involved the [Supreme] Leader’s pointed reinstatement of senior officials whom the president had dismissed, and other tensions over who would exercise the levers of power. It is generally felt that Ahmadinejad was significantly weakened by this series of events.”<sup>445</sup> This split could benefit the reformists, who would stand to gain during the upcoming Majles elections in March 2012.

## **1. Sanctions Impacts on the Iranian Petrochemical Sector**

A majority of the existing U.S. economic sanctions against the Iranian petroleum sector are contained in the Iranian Sanctions Act (ISA) and CISADA amendments.

Originally called the Iran and Libya Sanctions Act (ILSA), ISA was enacted to try and deny Iran the resources to further its nuclear program and support terrorist organizations... Iran’s petroleum sector generates about 20 percent of Iran’s GDP (which is about \$870 billion), 80 percent of its exports, and 70 percent of its government revenue.<sup>446</sup>

These sanctions target investment in Iran’s petrochemical infrastructure, as well as imported gasoline, which constitutes about 40 percent of Iran’s total consumption.<sup>447</sup> “[CISADA Amendments] tightened U.S. Sanctions in several areas and enacted numerous legal restrictions previously made under presidential executive orders.”<sup>448</sup> Six UN resolutions, critical of Iran’s nuclear program, have been specifically passed since 2006, but they do not specifically target the petrochemical sector.

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<sup>445</sup> Jones, *Succession and the Supreme Leader in Iran*, 112.

<sup>446</sup> Katzman, *Iran Sanctions*, 1.

<sup>447</sup> Ibid., 3.

<sup>448</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 116.

“Oil revenues represent the bulk of both government income and foreign exchange earnings in Iran, and thus give the officials and bureaucrats who control the petroleum industry disproportionate influence over the economy and the political system.”<sup>449</sup> Sanctions against this sector of the economy are designed to reduce short term and long term rents available to the Iranian government, thus reducing their ability to obtain resources for their nuclear program and support terrorist organizations.<sup>450</sup> However, higher than expected oil revenues are allowing for internal investment in the energy sector.

There is no doubt that sanctions have kept foreign investment in the countries manufacturing and energy sectors far below its potential. Oil revenues, however, have enabled the Iranian government to partially offset the shortfall in foreign investment by increasing domestic investment.<sup>451</sup>

Estimates of costs of sanctions to Iran from lost oil-related rents are around \$80 billion annually at \$100 per barrel,<sup>452</sup> which could, in turn, lower global oil costs by 10 percent if normalization of trade resumed.<sup>453</sup> Given that IMF projections of net oil revenues is \$64.4 billion for 2010–2011,<sup>454</sup> and that the lifting of sanctions would likely bring about further investment in Iran’s energy infrastructure, this cost is staggering, if accurate in its projections. Despite these sanctions and their effects on Iran’s energy sector, they have still not altered official Iranian nuclear policy.

## **2. Sanctions Impacts on the Iranian Financial Sector**

As discussed in Chapter II, financial sanctions have slowly gathered strength against Iran and seek to “disrupt Iran’s illicit activities... deter third parties from acting as enablers for Iran’s illicit activities...[and] force Iran to recalculate the cost-benefit ratio

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<sup>449</sup> Looney, *The Iranian Economy: Crony Capitalism in Islamic Garb*, 29–30.

<sup>450</sup> Katzman, *Iran Sanctions*, 1.

<sup>451</sup> Nader Habibi, *The Iranian Economy in the Shadow of Economic Sanctions* (Waltham, MA: Brandeis University: Crown Center for Middle East Studies, [2008]).

<sup>452</sup> Dean A. DeRosa and Gary Clyde Hufbauer, *Normalization of Economic Relations - Consequences for Iran’s Economy and the United States* (Washington, D.C.: National Foreign Trade Council, [2008]).

<sup>453</sup> Ibid.

<sup>454</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 98.

of—and consider continuing—its illicit activities.”<sup>455</sup> These efforts, while achieving economic costs, have not achieved political goals as “[Iranian] proponents of the nuclear program ... believe that pursuing it is well worth the sanctions, particularly since oil revenues in recent years have far exceeded the costs of the sanctions.”<sup>456</sup> Specifically, U.S. sanctions seek to limit Iranian access to the international financial sector by blocking U-Turn financial transactions in the U.S., and by the new authorities granted the U.S. Treasury in CISADA Section 104.<sup>457</sup> Blocking U-Turn financial transactions means U.S. banks cannot process Iranian financial transactions submitted by a third party, “effectively cutting off [Iran’s] ability to do business in dollars, the international currency for oil markets.”<sup>458</sup> Section 104 of the CISADA amendments of the ISA also seek to eliminate “Iran’s access to the international financial system [making] it more difficult for Iran to move its money.”<sup>459</sup> These efforts have been supplemented with informal efforts by the U.S. treasury department to sign on foreign banks to individually agree to reduce or eliminate their involvement clearing Iranian financial transactions due to the risks, on which 80 banks had agreed by April 2011.<sup>460</sup> These efforts have been so successful that President Ahmadinejad declared before the Majles, recently, that Iranian banks could no longer process international transactions.<sup>461</sup>

What costs are financial sanctions actually imposing on Iran?

The most important damage to the Iranian economy from the financial sanctions is due to the poor investment environment that has resulted. In the absence of the sanctions, Iran could have obtained much better terms [on energy investment projects via its buy-back contracts] and/or could have financed the oil projects by itself. It is tough to calculate the amount

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<sup>455</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 124.

<sup>456</sup> Habibi, *The Iranian Economy in the Shadow of Economic Sanctions*, 6.

<sup>457</sup> Katzman, *Iran Sanctions*, 27–28.

<sup>458</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 124.

<sup>459</sup> Katzman, *Iran Sanctions*, 28.

<sup>460</sup> Ibid.

<sup>461</sup> Thomas Erdbrink, “Ahmadinejad Admits Impact of Sanctions on Iran,” *The Washington Post* (1 November 2011), [http://www.washingtonpost.com/world/middle\\_east/ahmadinejad-admits-impact-of-sanctions-on-iran/2011/11/01/gIQAyBIacM\\_story.html](http://www.washingtonpost.com/world/middle_east/ahmadinejad-admits-impact-of-sanctions-on-iran/2011/11/01/gIQAyBIacM_story.html).

of damages to Iran's economy that has been specifically caused by the financial sanctions as various factors are involved and their costs unknown.<sup>462</sup>

In other words, financial sanctions make it difficult for Iran to get paid for their exports, raise the costs of borrowing, and limit investments that generate new revenues. Some varying analyses from the 1990s and early 2000s indicate that the total costs of financial sanctions to the Iranian economy each year was \$637 million during those years (via prohibition from ILSA investments, limits of economic assistance and loans, and oil swap and pipeline costs), with some estimates even higher.<sup>463</sup> When included with the additional costs of lost trade during this period (prohibition of U.S. exports and imports due to ILSA), costs were \$777 million each year.<sup>464</sup> Despite these seemingly large amounts, the ultimate effect on the Iranian GDP at the time was a little over a 1 percent reduction.<sup>465</sup> More recent analysis from 2008 indicates a much larger figure of sanctions impacts on Iranian trade, using new projection models.

On a combined basis, the impact of the US sanctions on Iran's total trade (exports plus imports) amounts to a loss of \$16.8 billion, or nearly 19 percent of Iran's actual total trade in 2005 (\$90.6 billion). Relative to domestic output, this total trade loss is equivalent to nearly 9 percent of Iran's gross domestic product in 2005.<sup>466</sup>

Therefore, despite the impact of financial sanctions, specifically, a difficulty processing transactions on the international financial market; reduction of investment; increased borrowing costs; reduction of trade and; a slight reduction of GDP, they have not altered Iranian policy.

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<sup>462</sup> Akbar E. Torbat, "Impacts of the US Trade and Financial Sanctions on Iran," *The World Economy* 28, no. 3 (March 2005), 421.

<sup>463</sup> *Ibid.*, 426.

<sup>464</sup> *Ibid.*

<sup>465</sup> *Ibid.*

<sup>466</sup> DeRosa and Hufbauer, *Normalization of Economic Relations - Consequences for Iran's Economy and the United States*, November 21, 2008, 10.

### 3. Legitimacy and Enforcement of Iranian Sanctions

Although UN resolutions and sanctions are not designed to decrease rents to the regime, they do confer an international consensus for implementing other Iranian sanctions (and unilateral sanctions among partner nations) due to worldwide concern with Iran's nuclear program.

Since 2007, Europe has been involved as the United States in diplomatic efforts to secure UN sanctions on dual-use items useful for Iran's nuclear and missile programs. By late 2010, U.S. sanctions on Iran were no longer an outlier; other major Western industrial countries imposed similar sanctions.<sup>467</sup>

Other countries and multinational corporations have thus decided that doing business with Iran is not worth the long term risks—and have pulled investments voluntarily. “Tehran's ability to do business as usual has taken a severe hit as banks, multinational corporations and insurers end their business relationships with Iran.”<sup>468</sup> This new-found sanctions legitimacy is a victory for the U.S., given its rocky history with Europe over unilateral sanctions in the 1990s via the ILSA sanctions and their extraterritorial effects.

U.S. allies have generally joined the Obama Administration's sanctions toward Iran, in part because the approach is perceived as not purely punitive and in part because their own concerns about Iran's nuclear advancement have increased ... [by] 2010, an unprecedented degree of global consensus has emerged on how to deal with Iran.<sup>469</sup>

Perhaps this aspect of the current sanctions regime has the most *political* leverage against Iran to alter its nuclear enrichment policy, more so than any financial or trade sanction can generate.

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<sup>467</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 117.

<sup>468</sup> Ibid., 125.

<sup>469</sup> Katzman, *Iran Sanctions*, 37.

## **B. WEAKNESS OF ACTUAL SANCTIONS ENFORCEMENT**

Despite the legitimacy and recent consensus of the latest rounds of UN sanctions, there are obstacles to their complete enforcement, and some reports indicate that these factors are significantly undercutting the effects of current sanctions.

By now, it is obvious that the U.S. sanctions of 2010, as well as the punitive measures adopted by America's partners against the IRI, appear to be less effective than initially expected... [Iran] has been able to mitigate their negative effect.<sup>470</sup>

The factors undercutting sanctions include: the weakness of partner nations' enforcement among their own private sectors, the role of China and lack of allied consensus.

### **1. Weak Private Sector Enforcement**

Iranian trade is shifting eastwards, away from Europe, with China becoming its largest trading partner, and one who is able to mitigate sanctions effects.<sup>471</sup> U.S. allies, whose governments supported the imposition of UN sanctions, also find it difficult to "ensure that [their] private sectors will not try and use any opportunity to continue economic cooperation with Iran or even bypass sanctions."<sup>472</sup> The withdrawal of multinational firms in trading and infrastructure development has also created a vacuum that is being filled by smaller companies among Iran's lesser trading partners<sup>473</sup> and the IRGC itself.<sup>474</sup>

The U.A.E. also faces difficulty curtailing its private sector's business enterprises with Iran, despite their government's initial embrace of UN sanctions over the summer of

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<sup>470</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>471</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>472</sup> Ibid.

<sup>473</sup> Ibid.

<sup>474</sup> Katzman, *Iran Sanctions*, 13.

2010.<sup>475</sup> Initially, the U.A.E. announced the freezing of Iranian persons' bank accounts operating within the U.A.E., a stricter Iranian export policy—getting tough on the export of dual-use items and refined petroleum,<sup>476</sup> and financial and insurance restrictions associated with exports to Iran.<sup>477</sup> These restrictions are reportedly having some effects on the Iranian business community, driving up the costs of imports in Iran by 15–30 percent, according to the Iranian chamber of commerce.<sup>478</sup> However, there is considerable pressure among the U.A.E. business community to lift the sanctions, and the authorities have not implemented the draconian embargo on refined petroleum exports to Iran, despite American calls to do so.<sup>479</sup> “The [U.A.E.] business community itself spares no effort to persuade U.A.E. authorities to secure economic ties with the IRI against the negative influence of the punitive measures.”<sup>480</sup> This is due to the significant involvement of Iranians in the U.A.E.'s own economy.

Close economic relations with Iran (from 2002 to 2008, the [Iranian] share of U.A.E. exports was around 15 percent), the existence of a large and influential Iranian community in the Emirates (from 300,000 to 800,000 people), as well as Iranian investments in the U.A.E. economy (around \$300 billion by 2008, one-fifth or so invested in Dubai trade malls), did not allow Arab business circles to support the UNSC or U.S. sanctions.<sup>481</sup>

Also, there are reports that other so called “Black Knight” companies (smaller firms of third countries that do not do business in the U.S., and therefore do not fear sanctions)<sup>482</sup> have stepped in to fill the void of withdrawing European companies to handle Iranian trade of sanctioned materials.<sup>483</sup> Besides the somewhat curtailed activity of the U.A.E., smaller firms from various countries such as China, India, Turkey,

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<sup>475</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15 .

<sup>476</sup> Ibid.

<sup>477</sup> Murphy, *Iran's Gateway in Dubai Highlights Sanctions' Bite*, 5 November 2011.

<sup>478</sup> Ibid.

<sup>479</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>480</sup> Ibid.

<sup>481</sup> Ibid.

<sup>482</sup> Ibid.

<sup>483</sup> Ibid.

Venezuela, Singapore, Japan, Ecuador, Brazil and Eastern European countries are stepping in to meet Iranian needs following the departure of Western businesses.<sup>484</sup> These needs include international shipping transit locations for sanctioned items and production of refined petroleum, and these firms are receiving varying levels of support from their governments to conduct this business with Iran, despite international sanctions.<sup>485</sup>

## **2. Impact of China**

“Between 2002 and 2008, total trade between Iran and China grew nearly eight fold ... it is the largest destination for Iran’s exports and the biggest source of Iran’s imports.”<sup>486</sup> China’s dependence on Iranian oil is growing considerably and there are few alternatives to meet this long-term need,<sup>487</sup> creating “opportunities for Tehran to bypass American sanctions.”<sup>488</sup> China, seeking to hedge its oil bets in Iran, is “striving to invest heavily in Iran’s energy sector,”<sup>489</sup> to include the “financing of the development of Iranian gas fields and road infrastructure.”<sup>490</sup> Chinese companies have also signed up to replace departing multinational firms previously invested in Iran’s energy sector who withdrew due to sanctions.<sup>491</sup> Although most of these deals are in the preliminary stages, and the backfilling firms are not as technically capable as the withdrawing firms,<sup>492</sup> strict banking sanctions against Iran are being avoided via the Chinese banking system.

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<sup>484</sup> Ibid.

<sup>485</sup> Ibid.

<sup>486</sup> Ilias, *Iran’s Economic Conditions: U.S. Policy Issues*, 25.

<sup>487</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>488</sup> Ibid.

<sup>489</sup> Ibid.

<sup>490</sup> Ibid.

<sup>491</sup> Ibid.

<sup>492</sup> Katzman *Iran Sanctions*, 49.



China's banks remain open to Iran<sup>493</sup> and "theoretically... allows them to make financial transactions not only with the PRC [Peoples Republic of China] but with other countries."<sup>494</sup>

China's status as a UNSC member also allows it additional room to grow its relationship with Iran.

Beijing is not going to support any sanctions against [Iran] except those imposed by the United Nations ... [and] China has traditionally spared no effort to emasculate UNSC resolutions so that they cannot create any problems for the developing cooperation between [them].<sup>495</sup>

### **3. Lack of Allied Consensus**

U.S. allies' appetite for sanctions is also waning, despite their government's initial support. South Korea relies on Iran to meet its energy needs, and is also maintaining its economic ties to Iran, despite supporting UN sanctions on Iran and imposing its own punitive economic sanctions against entities and individuals related to the Iranian nuclear program.<sup>496</sup> India also seemed to signal its support for sanctions, following President Obama's visit in November 2010 when India announced it would no longer use the Asia Clearing Union (based in Tehran) to handle overdue oil payment transactions, and that there were difficulties in finding an alternate payment mechanism.<sup>497</sup> However, payments resumed in March 2011 through a Turkish bank, and by September, Iran's central bank governor stated that India had paid its \$6.3 billion debt in full.<sup>498</sup>

The European Union's member states' participation in sanctions may also be faltering, despite their recent adoption of stronger sanctions. "In May 2011, the EU Council approved amendments to its sanctions, adopted in 2010, against Iran that made the European punitive measures even tougher. However, some evidence indicates that

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<sup>493</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>494</sup> Ibid.

<sup>495</sup> Ibid.

<sup>496</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>497</sup> Katzman, *Iran Sanctions*, 38.

<sup>498</sup> Ibid.

there is no unanimity among EU members.”<sup>499</sup> Due to the EU’s desire to find needed additional sources of natural gas, European companies have never completely cut their relationships to Iran and some are even considering moving businesses to neighboring countries (using local intermediaries as a business cover), or joining Chinese or Turkish firms as sub-contractors to avoid U.S. and UN sanctions.<sup>500</sup> So, while U.S. allies have joined up for additional sanctions, lending credibility and legitimacy to the sanctions regime, actual enforcement by their institutions has been weak, and full participation and cooperation by their private sectors has been sporadic—there is simply too much business and security at risk to completely sever ties with Iran.

### **C. SANCTIONS IMPACTS ON THE ACTORS IN THE POLITICAL ECONOMY**

Experts agree that sanctions are affecting the Iranian economy but not seriously hurting it.<sup>501</sup> “New international sanctions in 2010 have in practice increased the cost of doing business, limited FDI and technology transfer, and have affected international trade and financial transactions.”<sup>502</sup> These are precisely the broad effects desired. Yet real GDP continues to grow, largely the result of increased oil prices, at 3.2 percent for 2010/2011,<sup>503</sup> and medium term growth is expected at 4.5 percent on the continued strength of oil prices and efficiency gains from subsidy reductions.<sup>504</sup> This GDP growth continues, despite the high inflation rate (expected to be 23 percent in 2011/2012),<sup>505</sup> and a continued high general unemployment level of 14.5 percent in 2010<sup>506</sup> (25 percent among the youth).<sup>507</sup> UN sanctions are not much more effective. “The UN sanctions have

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<sup>499</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>500</sup> Ibid.

<sup>501</sup> Katzman, *Iran Sanctions*, 44.

<sup>502</sup> Anonymous, *IMF Country Report no. 11/241* (Washington, D.C.: International Monetary Fund, [2011]).

<sup>503</sup> Ibid.

<sup>504</sup> Ibid.

<sup>505</sup> Ibid.

<sup>506</sup> Ibid.

<sup>507</sup> Ibid.

a limited scope and focus on exports of goods and services that can directly contribute to Iran's nuclear program ... as a result of their limited scope, the UN sanctions have not imposed any severe costs on the Iranian economy.”<sup>508</sup> A dissection of sanctions impacts, analyzed in relation to one or more actor groups is, therefore, required to determine who or what actors in the political economy are being effected by sanctions.

### **1. Sanctions Effects on the Conservatives and Their Constituents**

The conservative clerical elite actors, as will be recalled from previous examination, broadly count the bonyads and bazaari merchants as client constituents and also have significant control over credit allocation among banking institutions. While economic sanctions are impacting these constituents, they are not weakening the political power of their conservative patrons, relative to the reformist actors.

Little specific information regarding the impact of economic sanctions on the bonyads is available, due to their opacity and quasi-state connection within the economy. However, due to recent analysis indicating the Iranian economy continues to grow thanks to higher oil prices (3.2 percent in 2010–2011),<sup>509</sup> these constituents are effectively shielded from the immediate effect of sanctions. An International Monetary Fund (IMF) consultation to Iran, during the summer of 2011, recommended increased privatization of small and medium enterprises across Iran (owned or controlled by the bonyads) and obtaining them listings on Tehran's stock exchange to “[gain] access to new capital, increase work incentives, and reduce pressures for bailouts and quasi-fiscal activities.”<sup>510</sup> The privatization of these quasi state-owned enterprises would also allow for the phasing out of subsidies and facilitate growth (including job creation), but “the [Iranian economic] authorities believed that more financing and government intervention might be needed for enterprise restructuring,”<sup>511</sup> reflecting their hesitancy to stray onto the Mullah's turf and alter the economic wealth base of these small and medium enterprises.

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<sup>508</sup> Habibi, *The Iranian Economy in the Shadow of Economic Sanctions*, 5.

<sup>509</sup> Anonymous, *IMF Country Report no. 11/241*, 5.

<sup>510</sup> Ibid.

<sup>511</sup> Ibid.

Sanctions effects against the bazaaris are unclear, but appear irrelevant due to high oil prices (i.e., not significant enough to bring about any change in the balance of power in the political economy). As previously mentioned, the bazaaris are feeling the sanctions pinch, but it is unclear (but most likely) that only the weaker and un-connected bazaaris are the most affected by them. The stronger and more politically connected bazaaris are most likely able to take advantage of smuggling networks (and use of the IRGC's ports). In October 2010, Iran's own president of the chamber of commerce mentioned that "sanctions were driving up the costs of imports by 15 to 30 percent."<sup>512</sup> Inflation was also discussed in Chapter III due to recent cash transfers in lieu of subsidies, and it was highlighted that this was eroding the wealth of many Iranian consumers and affecting the entire economy. Stricter enforcement of sanctions in the U.A.E. over the summer of 2010 has also led to Iranian bazaari importers turning to virtual loan-sharks and illicit shipping agents to move goods thru Dubai, being shunned by legitimate financiers and shipping agents, considerably raising their costs.<sup>513</sup> As a client constituency of the conservatives, there is no apparent change in their loyalty, despite the sanctions squeeze on import/export finished goods commerce, the bread and butter of the bazaaris. Their representation in parliament, the Motalefeh faction, is still staunchly conservative and loyal to the clerical elite. However, the uncertain business environment resulting from sanctions has caused some bazaaris to feel detached from this representation,<sup>514</sup> and the:

Bazaaris today seldom exhibit the [same] collective identity and public solidarity that occurred in past moments of Iranian political history. This stems partially from the new cleavages in bazaar networks that resulted from the [clerics] management of the economy and the picking of politically subservient economic winners. However, it also derives from significant changes in relations between the bazaar and the global economy.<sup>515</sup>

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<sup>512</sup> Murphy, *Iran's Gateway in Dubai Highlights Sanctions' Bite*, 5 November 2011.

<sup>513</sup> Murphy, *Iran's Gateway in Dubai Highlights Sanctions' Bite*, 5 November 2011.

<sup>514</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 109.

<sup>515</sup> Ibid.

## 2. Sanctions' Effects on the Neoconservatives and Their Constituents

The neoconservative elite, as will be recalled from previous examination, broadly count the state security services as client constituents and have a growing control over credit allocation among parallel banking institutions under their direct control. They also have growing control over the energy sector, with IRGC-affiliated companies taking a larger, if unclear, stake in energy sector development. "Some believe the August 2011 confirmation of Khatam ol-Anbia's chief, Rostam Ghasemi, as Oil Minister, will bolster the role of the IRGC in Iran's oil sector."<sup>516</sup> While economic sanctions are impacting their constituents, they are not weakening the political power of their neoconservative patrons relative to the reformist actors. Iran's recent inflation epidemic could conceivably negate the ability of the security services to be paid on par with inflation, thus eroding their loyalty. However, as discussed in Chapter III, it is likely these forces are both a priority for the regime (as in all authoritarian states, they are a pillar of the ruling elite), and have also gained a considerable degree of self-sufficiency, and are thus able to finance themselves (especially, the IRGC and affiliated organizations).

CISADA sanctions specifically target the IRGC and its affiliated business ventures, the key result being significant loss of foreign domestic investment within Iran. Iranian firms, themselves, do little business in the United States, so the effect on trade is limited to the reduction of foreign investment in Iran by foreign firms who wish to avoid being sanctioned themselves.<sup>517</sup> "U.S. officials in 2011 say that Iran has lost close to \$60 billion in investment as numerous major firms have either announced pullouts from some of their Iran projects, declined to make further investments, or resold their investments to other companies."<sup>518</sup> The NIOC and its subsidiaries and export affiliates (which are subordinate to the Iranian Oil Ministry) can also theoretically be targeted by ISA sanctions, despite the absence of a business exchange with U.S. companies.<sup>519</sup> But again, these sanctions effects are largely mitigated by high oil prices and the

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<sup>516</sup> Katzman, *Iran Sanctions*, 13–14.

<sup>517</sup> Katzman, *Iran Sanctions*, 13–14

<sup>518</sup> *Ibid.*, 48.

<sup>519</sup> *Ibid.*, 13.

government's ability to stimulate its own economic development and investment via these businesses by being awash in oil rents. By targeting these rents directly, it will be possible to "reduce [Iran's] ability to import needed technology for its WMD programs and enlist and maintain the loyalty of security personnel."<sup>520</sup>

Some sanctions against this actor are symbolic in their application. One CISADA sanction, from September 2010, prevents the obtaining of travel visas by IRGC officials who were complicit in human rights abuses to the U.S., and the EU also imposed similar sanctions in April 2011.<sup>521</sup> Further visa restrictions were issued in July 2011 by the U.S. and Britain, targeting 50 more "Iranian officials for participating in political repression in Iran."<sup>522</sup>

### **3. Sanctions Effects on Reformists and Their Constituents**

CISADA sanctions measures to support reformists exist, but are also not affecting the ability of reformists to gain economic or political strength relative to the other actors. Specifically, these seek to expand Internet freedom, limit Internet monitoring by the IRGC, increase U.S. broadcasting in Iran, identify companies selling media-monitoring software to Iran, and sanction regime officials who are involved in suppressing the reformists.<sup>523</sup>

Some of these efforts do have promise, such as measures to expand the reformists' (and the average Iranian's) use of the Internet and communication in Iran. These efforts are intended to not only broadcast the reformists' message to a wider audience, but to "to support the opposition's ability to communicate, [and] to reduce the regimes ability to monitor or censor Internet communications."<sup>524</sup> Additional measures seek to "increase U.S. broadcasting to Iran and to identify ... companies that are selling Iran technology equipment that it can use to suppress or monitor the internet usage of

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<sup>520</sup> Ibid., 48.

<sup>521</sup> Katzman, *Iran Sanctions*, 34.

<sup>522</sup> Ibid.

<sup>523</sup> Ibid., 32.

<sup>524</sup> Ibid., 33.

Iranians.”<sup>525</sup> Measures to freeze assets and ban travel of Iranian officials involved in human rights abuse/suppression of the opposition during the 2009 green movement uprising were implemented in CISADA and the European Union.<sup>526</sup>

Unfortunately, none of these sanctions appears to be strengthening the reformists economically (the elite patrons or their client constituencies—educated youth and intellectuals). They do not loosen the economic control of the conservatives or neoconservatives across the economy. What these sanctions do, as in the case of South Africa, is provide a significant amount of disapproval and international illegitimacy to the conservative clerics and the neoconservative security actors. As in the case of South Africa, perhaps this could be used as a spark to light the tinderbox and bring about further change, due to the indirect credibility heaped upon the opposition of the incumbent regime actors, in Iran’s case, the reformists. As international sanctions are more accepted and continue to mount, the governance capacity assessment of the incumbent regime is eroded internationally, especially regarding its economic performance (ability to create jobs, control inflation, provide basic commodities). This indirect legitimacy conferred upon the reformists can be harnessed to promote change based upon economic grounds, which could resonate among Iran’s disenfranchised.

#### **D. POSSIBLE MODIFICATIONS TO SANCTIONS AND OTHER ACTIONS**

As has been shown, current sanctions are having an economic effect but not the political one necessary to alter the structural power of capital power between the differing actor factions in Iran. The failure of sanctions to alter the power structure between the actors has resulted in no change in Iran’s nuclear or other contested policies. The conservatives and neoconservatives continue to control the majority of economic wealth and rents in the country and, therefore, continue to have the largest share of power and control within Iran. At best, sanctions have reduced the overall size of the economy and had some significant financial impacts, both in terms of delaying or preventing investment in Iran and reducing rents and economic activity. This section will look at

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<sup>525</sup> Ibid.

<sup>526</sup> Ibid., 33–34.

some possible ways to modify sanctions to possibly alter this power ratio, whether by reducing the economic wealth of the conservatives and neoconservatives and/or to separately grow the wealth of the reformist actors. The ultimate chances of economic and political success of these new efforts are difficult to determine, and their outcomes are uncertain. But, at the very least, they could alter the situational context in which the political actors compete over resources, although the outcome of these competitions is unknown.

### **1. Take Advantage of the Long-Term Economic Decline of Iran's Energy Infrastructure**

The Iranian energy sector may be more vulnerable than previously thought, of which current sanctions, internal political bickering, internal fear of foreign investment, a poor business environment, and inefficiencies in its own energy sector development are all exacerbating this long-term vulnerability.<sup>527</sup> The Iranian elite actors rely on energy sector rents, especially the conservative and neoconservative actors who use this revenue to fund targeted social programs for their constituents (i.e., the neoconservatives and cash handouts to the poor) or fund failing quasi-state companies (i.e., the conservatives and their funding of the noncompetitive bonyad-associated companies).<sup>528</sup>

Iran's ability to match its petroleum sectors' demand with supply is reflected in its inability to consistently match its OPEC production quotas.<sup>529</sup> This failure to attract new foreign investment in its oil and gas fields, due not only to sanctions, but mostly to Iran's unpopular buyback foreign investment program, is hurting the long-term maintenance of its oil exports.<sup>530</sup> "Iran's petroleum crisis is a strategic opportunity."<sup>531</sup>

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<sup>527</sup> Roger Stern, "The Iranian Petroleum Crisis and United States National Security," *Proceedings of the National Academy of Sciences of the United States of America* 104, no. 1 (2 January 2007), 377.

<sup>528</sup> *Ibid.*, 381.

<sup>529</sup> *Ibid.*, 378.

<sup>530</sup> *Ibid.*, 379.

<sup>531</sup> *Ibid.*, 381.



A lack of foreign investment, in both oil and natural gas fields and infrastructure across Iran, has led to a declining productivity of both.<sup>532</sup> This lack of investment is manifested in several areas, such as the increasing depletion rates of older fields—due to lack of investment of foreign reinjection techniques, refinery leakage from antiquated equipment, and a, lack of new projects to boost supply.<sup>533</sup> “NIOC has led no new major project since the 1979 Revolution.”<sup>534</sup>

Most of this lack of investment is due to Iran’s constitution, which prohibits foreign ownership and therefore offers unattractive buyback contracts to foreign investors, which are rarely taken, some of which are even rejected by “some more conservative element in Tehran ... if it believes the [NIOC’s] terms are too generous.”<sup>535</sup> Also, the IRGC’s GHORB is increasingly being brought in to make up the short-fall of investment in fields and infrastructure, but few details of financial or time-to-completion details can be found suggesting their technical capability is minimal.<sup>536</sup> As previously mentioned, other foreign firms’ investment (specifically from Asia) is also possible but “many such deals are said to be in preliminary stages, and clear examples of ‘backfilling’ are few to date. Most of the companies that might backfill abandoned projects are perceived as not being as technically capable as those that have withdrawn from Iran.”<sup>537</sup> Given this environment, “zero future foreign investment thus appears plausible.”<sup>538</sup>

Roger Stern’s 2007 study found that the net result of this lack of investment was a 10–12 percent decline rate in Iran’s petrochemical exports, culminating in their eventual export standstill and extinction, with the price per barrel ultimately determining the “when.”<sup>539</sup> “Oil recovery rates have declined, and, with no remedy in sight for the gas reinjection shortage, this decline may accelerate. Depletion rates have increased, and, if

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<sup>532</sup> Ibid., 378.

<sup>533</sup> Ibid.

<sup>534</sup> Ibid., 379.

<sup>535</sup> Stern, *The Iranian Petroleum Crisis and United States National Security*, 379.

<sup>536</sup> Ibid.

<sup>537</sup> Katzman, *Iran Sanctions*, 49,

<sup>538</sup> Stern, *The Iranian Petroleum Crisis and United States National Security*, 379.

<sup>539</sup> Ibid., 380.

investment does not increase, depletion rates will accelerate.” Lower oil prices will likely accelerate Iranian production to continue a short-term rent stream, while further accelerating the depletion rate of its fields and infrastructure. This further eliminates the long-term rents of the conservatives and neoconservative actors who control them.

*a. Recommended Actions and Chances of Success*

Existing U.S., UN, and other international sanctions are certainly doing their share of keeping out foreign investment. This, coupled with the fact that the capabilities of external backfill investment from both foreign third-party companies and IRGC affiliated companies are costly and incapable of restoring or expanding production, and are not nearly as capable, could lead to a near-term extinction of production, provided oil prices remain low.<sup>540</sup> When this would happen ultimately depends on the price of oil—higher oil prices keep demand on Iranian oil fields and infrastructure low, thus maintaining a slower level of exports and thus the status-quo in the Iranian political economy.

The best way to lower oil prices is to lower demand for Iranian oil, thus potentially bringing about a price attack, as happened to Saudi Arabia in the 1980s.<sup>541</sup> A reduction of Iranian oil demand could, conceivably, force Iran to cut its supply (and reduce any existing investment in its energy infrastructure further) and raise the prices of existing supplies to maintain its oil rents at previous income levels. Given the history of OPEC nations to cheat, it is conceivable that other OPEC nations could be negotiated with to continue to sell their oil at market prices to capture the lost Iranian market volume. Iran, observing its loss of market share and dwindling rents, would then rush to produce at the reduced market price, flooding the market with oil and further reducing the price and Iran’s revenues and its ability to invest and expand its energy infrastructure, and also accelerating the depletion rate of its oil fields and infrastructure.<sup>542</sup> However, reducing this demand will be extremely difficult to do, especially since China and other

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<sup>540</sup> Stern, *The Iranian Petroleum Crisis and United States National Security*, 380.

<sup>541</sup> *Ibid.*, 381.

<sup>542</sup> *Ibid.*

developing Asian nations are now Iran's largest oil export market.<sup>543</sup> Diplomacy in this case is unlikely to make headway in convincing China and other Asian states to voluntarily reduce their demand for (specifically) Iranian oil, but it is a remote possibility, and could have a significant payoff, if it worked.

Although difficult to achieve, the ultimate effect of these actions would be to reduce the investment in Iran's energy sector and achieve a near oil export extinction and thus significantly reduce the rents to the conservative and neoconservative actors who primarily control this sector of the economy. This would reduce their ability to dispense patronage to their constituency groups. This, in its own right, would destabilize the political economy and possibly strengthen the political hand of the reformist actors in the process—as their orientation for market-based reform could finally take root. Iran balances its external accounts at \$75 per barrel, and lower prices than this will destabilize its economy.<sup>544</sup>

## **2. Continue to Target Iran's Energy and Financial Sector with Multilateral Sanctions**

As mentioned, it is important to maintain existing sanctions, if only to keep out non-U.S. investors in the Iranian energy infrastructure. This is important and easy to justify, especially following the International Atomic Energy Agency's (IAEA) November 2011 report revealing “evidence to suggest that Iran may be pursuing nuclear weaponisation [sic] capabilities.”<sup>545</sup> This report, the first time the agency has issued evidence attesting to weaponization, has resulted in a new round of international sanctions, including sanctioning Iran's central bank.<sup>546</sup> Existing sanctions have significantly curtailed Iran's ability to clear oil payments in the international financial system, as well as reduced FDI in Iran's energy sector. Expanding multilateral and UN

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<sup>543</sup> Habibi, *The Iranian Economy in the Shadow of Economic Sanctions*, 5.

<sup>544</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 102.

<sup>545</sup> Anonymous, *Global Insight Country Intelligence Report: Iran*, Global Insight 2011.

<sup>546</sup> Ibid.

sanctions to further target Iran's energy and financial sector would further reduce rents to the conservative and neoconservative actors, and possibly reduce demand for Iranian (specific) oil.

*a. Recommended Actions and Chances of Success*

With this new IAEA finding, it is critical that diplomacy be used to expand and strengthen UN and multilateral international sanctions against Iran, with the goal of altering the status quo of the political economy. Expanded sanctions specifically targeting the Iranian energy sector and its ability to attract further investment, as well as expanded sanctions targeting the financial sector, and further reducing Iran's ability to process payments of its international oil rents, are perhaps the most visible, effective, and sellable forms of international pressure available. Sanctions that would embargo Iranian oil, thus raising the worldwide price of oil, are likely to have counter-productive effects both at home and abroad and would be opposed on principle.<sup>547</sup> But with the continued international concern regarding Iran's nuclear program, and the legitimacy of this new IAEA finding, this diplomacy and the expanded sanctions they bring about have a moderate chance of success. These actions further reduce rents that benefit (primarily) the conservative and neoconservative actors, which reduce their share of control in the Iranian political economy.

Another potential action to take along these lines is to destabilize the exchange rate of the Iranian riyal and create a financial panic that would hopefully lead to a political panic, destabilizing the conservatives and neoconservatives, politically. This is possible now that Iran's central bank has been sanctioned (by the U.S.) as of November 2011, which "plays a role in keeping Iran's currency stable."<sup>548</sup> This move, however, has humanitarian consequences that need to be considered as, "an unstable currency could harm Iran's ability to import some needed foodstuffs and medical products."<sup>549</sup> "Iranians are highly sensitive to the stability of the exchange rate because it has a direct impact on

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<sup>547</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>548</sup> Katzman *Iran Sanctions*, 29.

<sup>549</sup> *Ibid.*

the price of imports and people's confidence in the economy. Any fears regarding the foreign reserves of the country's central bank could easily spark a currency run and encourage people to hoard foreign currency."<sup>550</sup> The possibility of achieving this action unilaterally is low, especially given Europe's past opposition to sanctioning the central bank to begin with.<sup>551</sup> And, this action would not guarantee a winning situation for the reformist actors who would likely be just as affected by this action.

### **3. Fight and Win the Information War**

As discussed in Chapter II, examples can be drawn from the Iraqi and South African sanctions cases on the importance of utilizing the legitimacy of international sanctions to influence the actors we wish to promote. This legitimacy conferred from sanctions allows them to strengthen their own position in the political economy, thus achieving our policy goals. This can be done by fighting and winning the information dominance war—targeting the constituency clients and elites of the actors in a way that gives them the tools and courage they need to change the political economy themselves.

In Iraq's case, sanctions were used by Saddam to create and perpetuate a sense of being under siege by external enemies,<sup>552</sup> “which the regime exploited to deflect criticism from its rule and to justify its own repressive behavior.”<sup>553</sup> Sanctions also allowed Saddam to further solidify his control of the political economy due to the use of his co-opted smuggling networks. His control over imported goods allowed him to provide patronage to maintain the loyalty of his security forces and also appear as a provider to his people by dispensing aid from the oil for food program.<sup>554</sup> All the while, Saddam was able to win the information war over sanctions—and convince the world that Iraq was a victim of American aggression, versus due to his own policies and

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<sup>550</sup> Habibi, *The Iranian Economy in the Shadow of Economic Sanctions*, 6.

<sup>551</sup> Katzman *Iran Sanctions*, 29.

<sup>552</sup> O'Sullivan, *Shrewd Sanctions: Statecraft and State Sponsors of Terrorism*, 137.

<sup>553</sup> Ibid.

<sup>554</sup> Ibid.

actions.<sup>555</sup> Conversely, the United States' and the United Nations' efforts to counter this propaganda were feeble and uncoordinated and could have solidified support both internationally and among potential internal opposition.<sup>556</sup> "For sanctions to truly serve the purpose of regime change, they should have been coupled with other instruments—such as robust support for an effective opposition backed by regional actors—to form a coherent strategy to achieve that end."<sup>557</sup> These issues sound remarkably similar to the situation in Iran, and this formula sounds almost identical to what Iran needs.

In South Africa, the opposite effect occurred from sanctions. The strong, international consensus against apartheid gave rise to an international social movement that pushed for stronger sanctions and eroded the legitimacy of the regime.<sup>558</sup> This strengthened the hand of the black opposition group elites, giving them international legitimacy (e.g., Nelson Mandela), who would later credit their legitimacy benefits as one of the most important elements of their struggle. Although it was other economic forces (namely, the urbanization and collective bargaining of blacks as South Africa industrialized) that gave the opposition groups the economic base they needed in the political economy, the sanctions provided the elites with international and domestic credibility allowing for a unification of effort and agendas. The white Afrikaner regime had failed to effectively fight the information war and it was a significant part of its ultimate undoing.

*a. Recommended Actions and Chances of Success*

The U.S. and UN could make a more concerted effort to erode the legitimacy of the conservative and neoconservative actors by a sustained media effort that counters the regime's control of information—providing messages and themes that promote the reformist opposition leaders and/or agendas that are complimentary to U.S. desired policy. Current efforts are not enough and do not appear to be having much of a political effect, as the reformists' control of the political economy has not grown and

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<sup>555</sup> Ibid.

<sup>556</sup> Ibid., 157.

<sup>557</sup> Ibid., 158.

<sup>558</sup> Crawford and Klotz, *How Sanctions Work : Lessons from South Africa*, 9.

Iranian hardline policy has not changed. “Several measures to support the opposition’s ability to communicate, to reduce the regimes ability to monitor or censor Internet communications and to identify and sanction Iranian human rights abusers, were included in CISADA.”<sup>559</sup> Can more be done?

The Iran Freedom Support Act (IFSA, P.L 109-293), represented a congressional effort to promote the prospects for opponents to the regime. That law authorized “sums as may be necessary” to assist the Iranians who are “dedicated” to ‘democratic values ... and the adoption of a democratic form of government in Iran’, and ‘advocates the adherence by Iran to nonproliferation regimes.’<sup>560</sup>

However, as in past legislation (specifically, Speaker Gingrich’s very public announcement of an Iranian covert action campaign in 1995), it is likely intended to satisfy a domestic audience that something is being done against Iran. At the time, Gingrich pushed to have \$18 million added to the CIA’s covert action program on Iran as:

No one wanted to have to go before Congress and say that there was no CIA program against a country as troublesome as Iran, so the [Central Intelligence] Agency maintained one simply for the sake of it. The effort consisted mostly of anodyne efforts to introduce factually accurate information into Iranian news media and to expose Iranians to western culture.<sup>561</sup>

The conservatives and neoconservatives used this overt-covert action program for their own domestic propaganda purposes<sup>562</sup> and U.S. policymakers perhaps realized that achieving another Operation Ajax was unrealistic and even idiotic to ever attempt again. Yet, in concert with existing and expanded economic sanctions, a medium could be found in ensuring supportive themes and messages counter the regime’s propaganda on policies are sent, and if they not too extreme (advocating a violent overthrow of the regime), it

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<sup>559</sup> Katzman, *Iran Sanctions*, 32.

<sup>560</sup> Katzman, *Iran Sanctions*, 33.

<sup>561</sup> Pollack, *The Persian Puzzle: The Conflict Between Iran and America*, 274.

<sup>562</sup> *Ibid.*, 275.

would likely find positive international support. These messages could lend legitimacy and perhaps some credible support for the reformist actor elites.

#### **4. Harness Globalization and Compete with the IRGC's Control of Trade**

As has been shown in previous chapters, the conservative and neoconservative actors, via the IRGC, operates (and/or has coerced) smuggling networks that remain too opaque to effectively document. Due to their entrenchment in the Iranian political economy and their own ideological orientation, they will resist any diminishment of this control. Rather than continuing to sanction Iranian trade and isolate Iran from the global economy (which the IRGC simply smuggles through and controls to their own advantage), why not work with regional allies and attempt to establish new trade networks, ones that do not utilize IRGC-controlled ports or airports, and benefit some element of the reformist clients? As has been shown in previous chapters, there is a significant appetite for Western consumer goods in Iran. Sanctions are being utilized by the conservative and neoconservative elites, as in Saddam's Iraq, to control the rationing of goods as a form of patronage to their politically connected clients.<sup>563</sup>

The IRGC has a clear economic interest in a general sanctions regime... [it has] significantly weakened traditional players in the countries politics, such as the bazaar contingent ... as these players retreat from the Iranian market, the IRGC not only fills the economic vacuum they leave behind, but also gains their political influence.<sup>564</sup>

This trade to be opened up further would only be trade in consumer goods and could possibly go both ways following a vetting process by the Office of Foreign Assets Control (OFAC) of the trade deals. Consumer trade with Iran is currently minimal. "Total U.S.-Iran trade was about \$300 million in 2010 (\$208 million in exports to Iran, and \$94 million in imports) ... commercial sales of food and medical products have been allowed, on a case by case basis, and subject to OFAC licensing."<sup>565</sup> Deals involving dual-use

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<sup>563</sup> O'Sullivan, *Shrewd Sanctions : Statecraft and State Sponsors of Terrorism*, 137.

<sup>564</sup> Alfoneh, "All the Guard's Men: Iran's Silent Revolution," 78.

<sup>565</sup> Katzman, *Iran Sanctions*, 24.



items, trade with firms affiliated with the IRGC, items related to proliferation of weapons of mass destruction and technology and human rights abuse/travel restrictions would and should still remain sanctioned.

Trade losses occur mainly to Iran's exports of material manufactures (\$6.6 billion), foods (\$3.9 billion), and machinery and transport equipment (\$2.1 billion). As expected, these losses fall heavily on export shipments to the United States (\$1.3 billion) and the European Union (\$2.8 billion). But the largest proportion of the losses are spread over export shipment to a wide number of Iran's trading partners, including OPEC partners (\$5.5 billion), the Russian Federation (\$0.3 billion), and Japan (\$0.1 billion). In comparison, import losses to Iran from the US economic sanctions occur mainly to the country's imports of miscellaneous manufactures (\$0.6 billion), foods (\$0.3 billion), and beverages and tobacco (\$0.3 billion), and they fall particularly heavily on the imports in these categories from the European Union (\$0.4 billion) and the OPEC countries (\$0.3 billion).<sup>566</sup>

In other words, trade could be used as a means to build badly needed wealth among the reformist base, which could be translated into political power.

*a. Recommended Actions and Chances of Success*

By opening up consumer trade further from its current minimal extent among a new network of reformist-oriented business partners in Iran (preferably linked to a reformist patron cleric in particular), Iran could be better integrated to the regional economy, possibly eroding some of the control of the conservatives and neoconservatives over trade and patronage networks.

This would involve significant risk of loss, and its chances of success are slim since it would take time to build up these trade networks and alternate routes of supply—around the IRGC-controlled points of entry—would need to be found. Also, the guarantee that a reformist patron could provide long-term political cover (and control) of these networks does not exist. It would also require significant oversight of trade and U.S. businesses that OFAC is not likely staffed to provide.

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<sup>566</sup> DeRosa and Hufbauer, *Normalization of Economic Relations - Consequences for Iran's Economy and the United States*, 10–11.

## **5. Strengthen Sanctions' International Enforcement/ Extraterritorial Application**

As has been shown, U.S. unilateral ILSA sanctions, implemented since the adoption of UNSC Resolution 1929, have “significantly broadened American opportunities for exerting pressure on Iran.”<sup>567</sup> However, without more international support, “these measures appeared to be insufficient to influence Tehran to reconsider its approaches to the nuclear issue.”<sup>568</sup> In other words, they are failing to influence the political economy of Iran, and reduce the amount of control of the conservative and neoconservative actors in favor of the reformists.

The fact that four of Iran's major trading partners supported the American ILSA sanctions and even adopted their own punitive sanctions against Iran, is a significant diplomatic development.<sup>569</sup>

However, despite all attempts, the U.S. Government failed to persuade the People's Republic of China to follow the example of Iran's other major trading partners. This inability of the American authorities to make Beijing impose sanctions on [Iran], or at least follow the requirements of Washington concerning trade and economic cooperation with Tehran, has created a serious threat to the whole sanctions regime.<sup>570</sup>

Despite China's dependence upon Iranian trade, more must be done to pressure Beijing to support sanctions if there is any hope of their success, despite the U.S.'s “limited possible retaliatory measures”<sup>571</sup> available against Beijing to support.

More pressure must also be exerted on Iran's regional and European trading partners to eliminate selective implementation of sanctions by their enforcement agencies and avoidance of sanctions by their private sectors. Also, lesser trading partners of Iran (and firms among its private sector) such as Turkey, Venezuela, Ecuador, Brazil, and Eastern Europe must also cooperate by not filling trading vacuums left by departing firms

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<sup>567</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>568</sup> Ibid.

<sup>569</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>570</sup> Ibid.

<sup>571</sup> Ibid.

among Iran's major trading partners. Russian support is also not guaranteed. "In the aftermath of the recent Russian maneuvers in Georgia, Russian cooperation remains uncertain."<sup>572</sup>

Finally, convincing allies who support ILSA sanctions to also adopt extraterritorial sanctions would be an important development that further raises the costs of existing sanctions and UN resolutions. This would somewhat mitigate the effects of Chinese and other trade.

If, for example, the U.S. partners followed the American pattern and made their own sanctions extraterritorial (applicable to third countries, their entities and individuals), this would considerably raise the price of the violation of the sanctions and would certainly reduce the number of Tehran's loyal trading partners as well as black knights.<sup>573</sup>

*a. Recommended Actions and Chances of Success*

Strong diplomacy is the only course of action for these initiatives given the current global economic situation. The U.S. is already working closely with allies to cooperate with partners on sanctions and diplomacy has recently convinced some allies to adopt even stronger measures.<sup>574</sup> However, economic or trade pressure against allies (and their private sector violators) to support even further sanctions against Iran is limited and ill advised,<sup>575</sup> especially given the fragility of their involvement and support of Iranian sanctions to begin with. The U.S. state department must make the most of the recent International Atomic Energy Agency's (IAEA) November 2011 report finding, indicating Iran may be pursuing nuclear weapons.<sup>576</sup> This also remains the only avenue of approaching and gaining Chinese and Russian support for applications of sanctions.

The chances of diplomatic success, however, are extremely weak given that some partners' support of sanctions is extremely tenuous to begin with.

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<sup>572</sup> Habibi, *The Iranian Economy in the Shadow of Economic Sanctions*, 6.

<sup>573</sup> Kozhanov, *U.S. Economic Sanctions Against Iran: Undetermined by External Factors*, 15.

<sup>574</sup> *Ibid.*, 15.

<sup>575</sup> *Ibid.*

<sup>576</sup> *Ibid.*

As for countries deliberately creating opportunities for Tehran to bypass the American sanctions, it is no secret that it would be extremely difficult to make them change their position. On the one hand, the UNSC resolutions proved to be ineffective as a means of putting pressure on them. Moreover, due to the positions of China and Russia and some temporary members of the Security Council, the adoption of a truly efficient resolution is almost impossible.<sup>577</sup>

## E. CONCLUSION

Current economic sanctions against Iran are failing to alter the structural power of capital in Iran and thus achieve the intended political effects of altering the Iranian nuclear enrichment policy. This is due to the economic forces confronting them and sanctions inability to overcome these forces. They are failing to alter the political economy of Iran away from control by the conservatives and neoconservatives and towards the reformists. “Proponents [of Iran’s] nuclear program have had the upper hand, and they believe that pursuing it is well worth the sanctions, particularly since oil revenues in recent years have far exceeded the costs of sanctions.”<sup>578</sup>

A “net assessment” analysis of sanctions impacts to determine what impact sanctions are having on the Iranian political economy does not exist either. Neither the U.S. government nor any other international institution has completed a detailed analysis on sanctions impacts on the Iranian political economy, although academic estimates do exist regarding the economic impact of sanctions. Moreover, there remains disagreement among these actors as to sanctions’ exact goals.

Current sanctions broadly aim to affect three areas of Iran’s economy, but are still not enough to alter the structural power of capital and thus the Iranian enrichment policy: sanctions against Iran’s energy sector are deterring significant investment; financial sanctions are virtually stopping Iran’s ability to use the international financial system and; sanctions are lending a significant international consensus of legitimacy to the worlds’ position against the Iranian policy of enrichment.

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<sup>577</sup> Anonymous, *Global Insight Country Intelligence Report: Iran*, 2.

<sup>578</sup> Habibi, *The Iranian Economy in the Shadow of Economic Sanctions*, 6.

Analysis of this chapter indicates that economic sanctions against Iran are being undermined by several political and economic forces. Sanctions' biggest impediments to achieving their objectives are: they are not enforced properly among participating states and the international community; the trade relationships with Asian states, specifically China, and; contentious support for sanctions among allies. These factors are mitigating sanctions' impacts against the Iranian political economy and thus the political goals of altering the Iranian enrichment policy.

Possible modifications to sanctions and diplomatic initiatives that could be initiated are also unlikely to alter the structural power of capital in Iran away from the conservatives and neoconservatives, thus leading to reformists' gaining of an economic wealth base that could be translated to political power. While some appear promising and could bear fruit in the short term, it is unlikely that in the long term they could be sustained due to weak international participation and the inability of the reformist patrons to provide long term political protection for their new constituents.

## **V. THESIS CONCLUSION**

### **A. SUMMARY OF FINDINGS**

The thesis postulated that altering the control of the political economy of Iran in favor of the reformist actor group (and away from the conservative and neoconservative groups) was required to ultimately alter Iranian nuclear policy. The thesis further endeavored to show the failing role of sanctions against the Islamic Republic of Iran to accomplish this task, and attempted to postulate some alternative approaches to sanctions that could alter the resources or situational context of the differing actor groups competing for power in Iran.

#### **1. Framework of Analysis**

In presenting the argument of this thesis, five variables were first identified that could impact a sanctions regime's outcome (success or failure). This chapter will reexamine these variables in relationship to our reexamined Iran and attempt to validate the findings of sanctions' effectiveness relative to Chapter II. Several historical sanctions cases were briefly examined to determine sources of success or failure of sanctions regimes to achieve their political objectives relative to these variables. Iran was examined as a fragmented autocracy, while Iraq was examined as a unitary autocracy and South Africa as a democracy. These cases highlighted the importance of building an opposition political challenger in the target country, specifically one aligned (and willing to bring about) the sanctions' political objectives. Examination found that the most important strength of this opposition group was an economic base in the form of a client constituency. The South African sanctions regime success can be directly attributed to the growth of a political opposition, while Iraq's sanctions regime failure can also be attributed to the absence of the growth of such opposition.

The various political actors and their client constituencies in Iran were next examined, to include their interests, behaviors, and motives. Strengths and deficiencies of each group were noted, and areas of conflict and competition were highlighted to show

the degree of control of patronage networks between the patron actors and clients, which allowed for the greatest amount of political control. Finally, the relationships between actors and clients were examined to determine their vulnerabilities relative to the political competition within the Islamic Republic of Iran. Analysis found that the conservative and neoconservative actors had a firm political hold on Iran due to their significant economic constituency base, and the reformist actors had virtually no political hold due to their lack of a similar economic constituency base.

A detailed analysis of the sanctions regime against Iran was then presented, specifically including analysis of sanctions' effects against altering the balance of power within the Iranian political economy. Effects upon differing sectors of the Iranian economy were presented, along with an analysis of effects against each actor and their constituents. This analysis determined that sanctions were failing to effectively alter the economic wealth base of each actor in the political economy, and thus, no change in Iran's nuclear policy has been observed. Finally, possible modifications to sanctions were presented (along with corresponding diplomatic actions) to potentially bring about the necessary change in the political economy to see a resulting change in Iranian nuclear policy. The ultimate possibility of success of these new actions is difficult to determine. This thesis postulated that the new sanctions and diplomatic measures could potentially alter the situational context with which the actors compete over resources, but there remains the possibility of unintended outcomes from these changes in the political economy that may not work in favor of the political goals desired, specifically Uranium enrichment.

## **B. IRANIAN SANCTIONS REVIEW**

A brief reassessment of the five variables that impact the Iranian sanctions regime's ability to bring about a desired political outcome is necessary, this time factoring in the actor-centric analysis and sanctions' effects developed in Chapters III and IV. Findings largely confirm the earlier analysis from Chapter II.

## **1. Sanctions Remain Inadequate**

Chapter II found that sanctions were inadequate to meet the economic and political goals of altering Iranian behavior, specifically nuclear enrichment. A reassessment of Iranian sanctions, factoring in the extent of control of the political economy of the conservative and neoconservative actors, as well as the limited effects the sanctions are actually having to alter this balance of power, continues to find that sanctions are inadequate to sufficiently alter the political economy and thus Iranian policy and behavior. However, sanctions are achieving their intended economic effects. Specifically, they are reducing investment in the Iranian energy sector, as well as rents from it, reducing Iran's ability to conduct transactions across international financial markets, reducing trade and Iran's GDP. These effects are not enough to alter the asymmetric power balance between the actors, though, and control of the political economy resides with the conservatives and neoconservatives, and the reformist actor group is not benefiting from the economic impacts of sanctions.

## **2. Mixed Effects of Legitimacy Persist**

An initial analysis of sanctions from Chapter II found they were having a mixed effect relative to their legitimacy. Domestically they were conferring legitimacy to the conservative and neoconservative actors due to their portrayal of sanctions as an external threat against inherent Iranian rights, while internationally they solidified a significant degree of worldwide consensus against Iranian enrichment. Analysis from Chapter III showed that the conservative and neoconservative actors are increasing their control and monitoring of Iranian media outlets (especially the Internet and social media), and analysis from Chapter IV showed that U.S. CISADA sanctioning efforts to mitigate this media control to assist the reformists was inadequate. Chapter IV also showed that the recent imposition of additional sanctions were the result of a renewed consensus of



worldwide concern over Iran's nuclear enrichment policy, thus confirming the illegitimacy of the ruling regime. Therefore, in the final analysis, the effects of sanctions continue to remain mixed—inadequate to confer the needed domestic legitimacy to the reformists as an internal opposition group, but adequate to confer worldwide consensus against enrichment.

### **3. Enforcement of Sanctions Remain Weak**

Initial analysis from Chapter II showed that sanctions enforcement was improving but continued to be undermined by regional and global trade, especially with China. Additional analysis from Chapter IV confirmed these findings, and also specifically found that actual enforcement of sanctions among allies' private sectors is not as strong as it could be, and that there was a lack of consensus of sanctions among allies participating in sanctions due to their own national interests. Therefore, in the final analysis, there is significant room for improvement in sanctions enforcement, as in actual practice, it is weak.

### **4. True Popularity of Sanctions is Difficult to Gauge**

Chapter II showed that sanctions have gained a much wider level of international support, at least at the highest policy levels, due to legitimate concerns over Iran's enrichment program. While this is true at the governmental policy level, additional analysis from Chapter IV shows that the degree of this popularity and sanctions enforcement is not as significant as at first glance. European consensus of sanctions is far from universal, and sanctions among Iran's regional and Asian trade partners remain unpopular. This unpopularity among the private sectors of participating states has led to the backfilling of investment in Iran, as well as weak enforcement of sanctions among the governing institutions of states pledged to support sanctions. Therefore, in the final

analysis, the international popularity of sanctions is certainly not as steadfast as initially thought, and not enough to ensure conference of legitimacy to the reformist actors as was seen in the South African sanctions case.

## **5. Entrenched Actors Control the Structure of the Iranian Political Economy**

The analysis in Chapter II indicated that the structure of the Iranian political economy was the ultimate inhibitor to sanctions' effectiveness. Implied was that since the conservatives and neoconservatives controlled the sources of wealth, the reformists could not gain economic wealth, at their expense, and thus gain political power as well. The conservatives' and neoconservatives' control of the economy has allowed them to emasculate most of the private sector, making it dependent upon the state for work and revenues. More in-depth analysis from Chapter IV indicates that sanctions are failing to alter this structure, primarily due to the high level of petrochemical sales to China, Iran's largest trading partner. These sales allow the conservatives and neoconservatives to continue their patronage networks to the client constituencies, allowing them to maintain control of the political economy. Weak enforcement of existing sanctions also plays a part in maintaining the conservatives' and neoconservatives' control of the structural power of capital in Iran, and thus the political economy.

However, this does not mean sanctions have been completely ineffective. Sanctions have reduced the rents to the actors, and the size and strengths of the Iranian economy, and have isolated Iran, diplomatically from the international community. This isolation and greater dependence upon petrochemical rents (due to sanctions) has very likely caused the increased competition among the actors within the political economy, as

witnessed recently (December 2011) with “divisions deepening between Supreme Leader Ayatollah Ali Khameni and President Mahmoud Ahmadinejad and his allies.”<sup>579</sup> In other words, sanctions have indirectly increased competition between the actors for control of institutions and government offices to control greater rents. But the sanctions’ bite has not been great enough (primarily due to continued Asian petrochemical sales and weak sanctions enforcement) to cause this competition to crescendo into a coup d’état, constitutional crisis, or velvet revolution that would remove the conservatives from their position as the ultimate power brokers, or more specifically, removing the supreme leader from his office and replacing him with a neoconservative military cabal or clerical puppet of this actor group.

### C. IMPLICATIONS

Chapter IV examined new sanctions’ modifications and diplomatic initiatives that could be introduced to alter the political economy in favor of the reformist actor group, and found that their ultimate chances of success were difficult to determine, but that they could perhaps alter the situational context with which the actors compete over resources. This ambiguity, however, is very likely not going to be enough to achieve the political goals of the Iranian sanctions regime. Economic sanctions that do not threaten the survival of the incumbent actor(s) in office (i.e., alter the political economy),<sup>580</sup> or at least generate significant political costs to those actors, will ultimately fail.<sup>581</sup>

The leadership would only concede if the cost of noncompliance exceeds the cost of granting the sender’s demands. For coercion to work, the political stability of the target should suffer more from coming under pressure than from conceding. The sender has some costs for imposing sanctions. Because of this, the sender would only engage in sanctions when it believes that there is some chance the target will concede.<sup>582</sup>

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<sup>579</sup> Shirin Ebadi, “Behind the Islamic Republic’s Bluster,” *Wall Street Journal* (30 December 2011). [http://online.wsj.com/article/SB10001424052970204464404577116734013838136.html?mod=googlenews\\_wsj](http://online.wsj.com/article/SB10001424052970204464404577116734013838136.html?mod=googlenews_wsj).

<sup>580</sup> Nikolay Marinov, “Do Economic Sanctions Destabilize Country Leaders?” *American Journal of Political Science* 49, no. 3 (7 July 2005), 564.

<sup>581</sup> *Ibid.*, 566.

<sup>582</sup> *Ibid.*

It has been shown in the research of this work that defined political goals of the Iranian sanctions regime cannot be agreed upon among both international (and even U.S. domestic) bodies. Therefore, the findings of this research indicate that until the exact political goals can be defined by all participating states, Iranian sanctions will remain inadequate; will fail to confer sufficient legitimacy on the reformist actors in Iran; will remain weakly enforced; will remain unpopular among the private sector with a questionable level of participation, and; will not alter the Iranian political economy in favor of the reformist actors. Therefore, the ultimate goal of the sanctions regime should be to help usher in the reformist actors to power in Iran—without an Operation Ajax style coup d'état—who would bring about the desired political goals of the sanctions regime. This is a difficult but not impossible task. Achieving the ultimate political objective of the sanctions regime (cessation of Uranium enrichment) is achievable because of the makeup of the political economy as a fragmented autocracy, provided sanctions could be designed in such a way as to strengthen the reformists while weakening the conservatives and neoconservatives. This thesis argues the following actions should be taken to achieve this goal.

### **1. Binding UN Resolution Defining the Exact Political Objectives and Matching Sanctions**

Since 2006, the U.N. Security Council has passed six resolutions critical of Iran for its controversial nuclear program. Each resolution was designed to increase pressure on Tehran to suspend its uranium enrichment, and ballistic missile development programs, two of three critical steps in obtaining a nuclear weapons capability.<sup>583</sup>

While defining the cessation of nuclear enrichment as the goal is part of this step, a clear matching of sanctions tasks to achieve this objective remains incomplete in the international forum (i.e., current sanctions are inadequate to achieve this objective as they do not impose sufficient political costs to the conservative and neoconservative actors pushing the enrichment policy). Therefore, the adoption and enforcement of binding international sanctions that most effectively achieves this goal is necessary. “The UN

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<sup>583</sup> Wright et al., *The Iran Primer: Power, Politics, and U.S. Policy*, 119.

sanctions have a limited scope and focus on exports of goods and services that can directly contribute to Iran's nuclear program.”<sup>584</sup> As has been shown in Chapter IV, U.S. unilateral sanctions, while more effective in imposing financial costs, are insufficient to achieve this objective alone. The body of states imposing the sanctions must recognize that the conservative and neoconservative actors in the Iranian political economy will not alter their enrichment policy and, therefore, the sanctions regime must seek to specifically weaken their economic constituency base, while simultaneously strengthening the reformist actor's constituency base. Diplomacy is the only way to achieve this binding UN resolution, but as has been shown in Chapter IV, will be difficult to achieve given Iranian trade relationships and the dependence upon Iranian oil by some sending states. “In the near future, the continuation and effectiveness of the UN-sponsored sanctions will remain hostage to the state of U.S.-Russia and U.S.-China relations.”<sup>585</sup> Therefore, the possibility of the UNSC passing such a binding resolution is extremely low.

## **2. Embargo Iranian Oil and Tolerate the Long-Term Economic Costs**

As has been shown in previous chapters, unfortunately the costs of even the most effective international sanctions regime can be tolerated by the conservatives and neoconservatives due to Iran's sales of oil. “Despite long-standing U.S. sanctions, Iran's oil revenue is expected to rise by a third this year to U.S. \$100 billion.”<sup>586</sup> Therefore, in order to bring about a lasting change in the political economy, these sales must be embargoed, as was seen in Iraq prior to 1996.

This move is not without risk and cost, but is necessary. “Such an embargo would constitute the most direct economic confrontation yet between Iran and the West and would amplify tensions as Iran repeatedly threatens to close the Straits of Hormuz (SOH),

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<sup>584</sup> Habibi, *The Iranian Economy in the Shadow of Economic Sanctions*, 5.

<sup>585</sup> Habibi, *The Iranian Economy in the Shadow of Economic Sanctions*.

<sup>586</sup> Yadullah Hussain, “Sanctions Against Iran could Trigger Oil Price Spike,” *Financial Post Magazine* (19 December 2011), 23 December 2011.

through which passes about one-fifth of the world's oil supply.”<sup>587</sup> Should this oil supply come under threat, whether from embargo or from the closure of the Straits of Hormuz due to military conflict, the international oil markets would respond with a price spike. “The result could be catastrophic. Oil prices could jump U.S. \$23 a barrel in the first few weeks of the conflict and by a jaw-dropping U.S. \$175 if it persists, according to a survey of energy traders by Rapidan Group, a Washington-based consultancy.”<sup>588</sup> Military postures in the U.S. central command area of responsibility must anticipate this threat and be prepared to forcefully open the SOH militarily. But how long could sanctions-sending states tolerate a sustained near-doubling of world oil prices? However, the ultimate effects of an Iranian oil embargo and their effects on world oil prices remain unknown, especially as other OPEC countries have pledged to make up for the loss with spare capacity.<sup>589</sup> Still, there is a difference between what can be done and what is required. “Iran produced about 3.56 million barrels a day in November, according to data compiled by Bloomberg News. That’s more than the 3.12 million barrels a day of spare capacity available among OPEC producers.”<sup>590</sup>

Other OPEC states are working on ways to mitigate an Iranian supply loss but there is no guarantee that they would or could make up the full difference, even if they operated at full capacity.<sup>591</sup> Also, there is no guarantee that Asian states (especially China) will not continue to buy Iranian oil, further increasing the need for diplomacy to ensure participation among Iranian energy-dependent states to have an economic impact

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<sup>587</sup> Jay Solomon et al., “U.S., Allies Step Up Iran Embargo Talks,” *Wall Street Journal*, sec. Business, 19 December 2011.  
<http://online.wsj.com/article/SB10001424052970204058404577106544032326610.html>.

<sup>588</sup> Ibid.

<sup>589</sup> A. R. Lakshmanan and Asjylyn Loder, “U.S. Joins EU in Push for Iran Oil Embargo in Effort to Stop Nuclear Plans,” *Bloomberg* (21 December 2011), 1 January 2012.  
<http://www.bloomberg.com/news/2011-12-21/u-s-joins-eu-in-push-to-reduce-iran-s-sales-of-oil-over-nuclear-program.html>.

<sup>590</sup> Ibid.

<sup>591</sup> Solomon et al., *U.S., Allies Step Up Iran Embargo Talks*.

on Tehran.<sup>592</sup> Therefore, the potential for the worst-case scenario (a substantial increase in the price of oil) must be accepted among imposing states to achieve the desired political outcome.

### **3. Tolerate Humanitarian Costs of the Sanctions Regime**

The international sanctions regime adopted, including the oil embargo, must be strictly enforced, and the financial costs to the sending states (along with the humanitarian costs to the Iranian populace) must also be tolerated until the political objectives are achieved. As will be recalled from Chapter II, the Iraqi oil embargo very nearly succeeded in eroding Saddam's unitary control of the political economy prior to the humanitarian concerns that led to the oil for food program. The adoption of the oil for food program, based on humanitarian concerns due to Saddam's effective control of propaganda, gave his regime an out—focusing the bulk of his limited resources on expanding his patronage networks and solidifying his unitary control of the political economy against rivals instead of being focused on feeding his population. His efforts showcased the suffering of the average Iraqi due to the effects of sanctions, versus from his own economic policy choices. Saddam had no intention of complying with the political goals of the sanctions regime against him, and only his removal from power would achieve the political objectives. The same situation can be inferred to be true in Iran, given the multiple statements between the conservative and neoconservative actors indicating they will never bow to the political or economic pressure of sanctions.

As identified in Chapter IV, fighting and winning the information war is half of this battle. Iranian propaganda efforts will likely result in the same portrayal of suffering of the average Iranian citizen due to sanctions. Efforts must be made to counter this Iranian propaganda across the international community, instead showing that humanitarian costs are really due to the economic choices of the conservative and neoconservative actors. This information campaign could mitigate the calls for repeal of the sanctions regime that is effectively pressuring and weakening the conservative and neoconservative actors. However, a humanitarian crisis would eventually come to pass

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<sup>592</sup> Ibid.

and the international community must be prepared to accept this and stick with the sanctions regime until Iranian political objectives have been achieved.

#### **4. Undertake More Effort to Promote the Reformist Actors**

Research has shown that current sanctions efforts targeting the Iranian energy sector (reducing investment in the energy sector) and the Iranian financial sector (reducing rents to the Iranian government) are working to ultimately weaken the conservative and neoconservative actors. But more effort must be made to simultaneously strengthen the reformist actors, relative to the other actors, in the political economy. Thesis research has shown that the sanctions efforts are failing to provide needed domestic legitimacy to the reformist actors within Iran, mostly due to the portrayal of the sanctions regime as being imposed by the external enemies of Iran. This is due to the fact that the conservatives and neoconservatives are able to avoid the costs of sanctions with the sales of oil via their control of the political economy, and keep the economy running and avoid criticism and questioning of their own legitimacy. Without more economic problems, the conservative and neoconservative actors will be able to use oil revenues to “generate enough economic trickle-down to keep discontent at bay.”<sup>593</sup> However, economic problems persist and contribute to infighting among the actors, reflected by the worsening inequalities among their constituencies.

The conservatives and neoconservatives face legitimacy problems with ongoing high inflation, unemployment, and a destabilized currency (due to sanctions and a perception of the inability to effectively provide a solid macroeconomic solution)<sup>594</sup> that could indirectly help the reformist actors, but this may not be enough to alter their relative power position. Steps are being taken to mitigate these economic deficiencies, although specific successes are hard to point out. Inflation is being fought with tighter credit and fiscal policies by the central bank,<sup>595</sup> as well as administrative efforts such as

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<sup>593</sup> Looney, *The Iranian Economy: Crony Capitalism in Islamic Garb*, 33.

<sup>594</sup> Rick Gladstone, “As further Sanctions Loom, Plunge in Currency’s Value Unsettles Iran,” *New York Times* (20 December 2011), 30 December 2011.

<sup>595</sup> Anonymous, *IMF Country Report no. 11/241*, 11.



“numerous price measures, such as price monitoring and enforcement of price transparency and the accumulation of inventories,”<sup>596</sup> but the official Iranian inflation rate of 20 percent is likely much higher by outside estimates.<sup>597</sup> Unemployment is a serious concern, especially among the youth. “To achieve higher growth and create jobs, the authorities have adopted a comprehensive multi-pronged strategy ... [aimed] at promoting a market based economy by reducing the role of government, privatizing enterprises, and increasingly allowing prices to reflect market forces.”<sup>598</sup> This complements other efforts to increase FDI, reduce subsidies, and provide adequate unemployment benefits and job training to their labor market.<sup>599</sup> Despite an allowance by the regime to allow their currency to depreciate by 11.5 percent in the summer of 2011,<sup>600</sup> the rial plunged in value to its lowest level in history against the dollar, by December 2011, due to these ongoing economic problems, isolation from sanctions, and a perception that government officials are incapable of finding a solution.<sup>601</sup> A rapid rise in both gold prices and the number of monetary exchange bureaus offering currency exchanges at unofficial rates has also been witnessed in recent months.<sup>602</sup> However, while these problems have increased infighting among the actors, the makeup of the power structure within the political economy has not changed. The fact that oil prices remain far above the break-even amounts for budget and current accounts (\$75 and \$60 per barrel, respectively)<sup>603</sup> “has helped improve the current account and budget surplus,

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<sup>596</sup> Ibid.

<sup>597</sup> Gladstone, *As further Sanctions Loom, Plunge in Currency's Value Unsettles Iran*, 30 December 2011

<sup>598</sup> Anonymous, *IMF Country Report no. 11/241*, 15.

<sup>599</sup> Ibid.

<sup>600</sup> Anonymous, *IMF Country Report no. 11/241*, 15.

<sup>601</sup> Gladstone, *As further Sanctions Loom, Plunge in Currency's Value Unsettles Iran*, 30 December, 2011.

<sup>602</sup> Anonymous, *IMF Country Report no. 11/241*, 8.

<sup>603</sup> Ibid.

and maintain comfortable international reserves.”<sup>604</sup> In other words, high oil revenues continue to mitigate other economic problems that would normally hobble political actors in other political economies.

Research in Chapter IV has identified several measures that could be taken to strengthen the economic and political base of the reformist actor’s constituencies, including harnessing global trade to compete against the conservative and neoconservatives’ control of the consumer goods trade and using more robust efforts to promote the domestic legitimacy of the reformists. Another potential action to weaken the legitimacy of the conservative and neoconservative actors is to use financial sanctions against the Iranian central bank to destabilize the exchange rate leading to a financial panic and political crisis. While the chances of success (and exact effects) of these actions remain unknown, they are perhaps the only (and best) chances of changing the control of the Iranian political economy that exists, short of armed conflict.

#### **D. CONCLUSION**

The findings of this thesis indicate that if the international community is concerned about the Iranian nuclear program (among other Iranian policy concerns) and wishes to use economic sanctions (not armed conflict) to change these policies, it must adopt stronger economic sanctions that alter the asymmetric balance of power in the Iranian political economy. Current economic sanctions, while having some economic effect, are not able to alter the Iranian political economy due to the conservative and neoconservative control of the political economy and institutions, and external petrochemical sales which solidify this control. Thus, Iran continues to enrich Uranium and ignore UN resolutions and international sanctions calling on it to cease this activity.

Iranian enrichment activity continues to be a worldwide concern, and appears to finally be solidifying a consensus for additional sanctions to cause Iran to abandon this activity. Within the Persian Gulf, tensions with the Arab states continue to mount,

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<sup>604</sup> Ibid.

although it has been shown that some of these states remain large Iranian trading partners. Despite this, a U.S. and coalition military commitment to the defense and training of GCC states continues.

Recently adopted sanctions efforts promoted by Mark Dubowitz, Director of the Iran Energy Project at the Foundation for Defense of Democracies, who advises the U.S. congress and U.S. administration on Iranian sanctions, calls for diplomacy to divest U.S. allies (Japan, South Korea, Turkey, Europe, etc.), from buying Iranian oil, thus purchasing it elsewhere—leaving India and China (as the remaining purchasers) to collectively bargain down the price of Iranian oil and reduce oil rents to the regime.<sup>605</sup> In the author's opinion, these efforts could have some success in reducing Iranian oil rents, but at what rate is still highly unpredictable (due to an assumption of Chinese, Indian, and other states' collusion with the program), which could have other unintended consequences, which can briefly be examined by the established framework developed earlier.

In the author's view, these sanctions will remain inadequate without a solid commitment by the participating states (and their private sectors and enforcement agencies) to abide by the new embargo, as well as a solid commitment by the non-participating states to agree to collectively bargain down the price of the remaining Iranian oil supply available. Without these solid commitments, rent reduction available to the Iranian conservative and neo-conservative actors will be minimal, and will likely enhance a large smuggling syndicate of Iranian oil as was seen during the years of Iraqi sanctions that would take massive law enforcement efforts to contain. The author can find no such commitments from the non-participating states as of the writing of this work, and these new sanctions remain only in the discussion phase among potential participating states. Therefore, these new sanctions would not only continue to be inadequate to alter the Iranian political economy, but could also generate potentially huge unintended consequences.

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<sup>605</sup> Lakshmanan and Loder, *U.S. Joins EU in Push for Iran Oil Embargo in Effort to Stop Nuclear Plans*, 1 January 2012.

Legitimacy effects of this new proposed sanctions regime, both internationally and domestically in Iran, could also suffer. Unless there is a solid commitment with participating states (to abide by and enforce the embargo) and non-participating states (to collectively bargain down the price of Iranian oil), the sanctions would not be seen as completely legitimate internationally. Also, within Iran, the conservatives and neo-conservatives would continue to frame the sanctions as an attack on Iranian sovereignty (as was done successfully in Iraq). Without a massive capability to counter this Iranian domestic and regional propaganda, regional and domestic public opinion could possibly be swayed in the conservatives and neo-conservatives favor (as was also seen in Iraq by Saddam). As has been seen in the past, the first victims of punitive sanctions are the population of the target state, and their suffering would likely be used as a propaganda tool. Therefore, the legitimacy effects of this proposed embargo are likely to backfire without a firm commitment of participating and non-participating states, as well as a massive information operations campaign that complements the embargo to delegitimize the Iranian conservative and neo-conservative actors domestically (and regionally).

Enforcement of current Iranian sanctions is already weak, and therefore enforcement of a voluntary embargo (without a UN mandate) would be extremely difficult and would require considerable diplomacy and enforcement cost. As was witnessed during the Iraqi sanctions episode—smuggling syndicates found numerous ways to bypass international enforcement—allegedly coopting even officials of the United Nations—on their way to pass thru or supplying states who were supposed to be participating in their enforcement. All this smuggling activity occurred during a time period of decreasing oil prices as well (late 1990s) and had the legitimacy and blessing of the United Nations. Therefore, assuming Mr. Dubowitz (Director of the Iran Energy Project at the Foundation for Defense of Democracies) is correct—and non-embargo participating states would be able to collectively bargain down the price of oil and international oil prices remain stable or decline—the conservative and neo-conservative actors will very likely take a page from Saddam’s playbook and begin to foster smuggling syndicates to export their oil to maintain their rents. The key here is the word

voluntary—stopping this smuggling activity will be much easier with the legitimacy and support of a UN mandate to do so than without.

As the true popularity and international consensus of current Iranian sanctions is difficult to gauge among participating states, at least one aspect of a voluntary embargo would be beneficial—participating states would certainly not voluntarily join unless it was in their interest (and their constituencies/private sectors interest) to do so. This is not to say that voluntarily joining the proposed embargo would not involve costs, but that the benefits of joining would outweigh such costs. Therefore, the voluntary embargo proposal of new Iranian sanctions would certainly serve as a convenient litmus test, state by state, for their true popularity and would make the identification of their support easier to gauge.

Finally, these sanctions also still fail to alter control of the Iranian political economy away from the conservatives and neoconservatives, and thus alter their nuclear enrichment policy. This is due, primarily, to the determination of these actors to enrich Uranium as a national priority, the sanctions' inability to seriously weaken these actors' entrenchment in the political economy and the sanctions' inability to lend economic support or legitimacy to reformist actors as an alternative political opposition. Oil markets are likely to respond with increased prices also, despite the theoretical proposition that no supply is actually being lost. Indeed, oil futures prices in New York had already inched up in response to this announcement of a potential divestment of Iranian oil by participating European states.<sup>606</sup>

Should sanctions start to take effect and alter the political economy, seriously weakening the conservative and neoconservative actors' hold, it is conceivable that a trade of Uranium enrichment for a cessation of sanctions could be made by Tehran. The primary interest of these actors is survival; therefore, this program is ultimately expendable. But the rate of erosion of this control is unpredictable (and it has been shown that net assessments of sanctions' economic effects do not exist) and, in the author's view, it is best not to stop a sanctions regime at such an offer. As seen in the Iraqi

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<sup>606</sup> Lakshmanan and Loder, *U.S. Joins EU in Push for Iran Oil Embargo*.

example—when sanctions bit and Saddam negotiated the oil for food program—his regime did not hesitate to cheat on the sanctions to ensure remaining in power at any cost. This lesson must not be lost on policymakers today, and the Iranian actors will likely follow the same trend—reconsolidating control of the political economy once the sanctions regime has ended and, eventually, reconstituting clandestine Uranium enrichment. The economic sanctions, and other efforts (diplomatic and other), must ultimately erode the power of the conservatives and neoconservatives, while promoting the reformist actors in the political economy to its ultimate control to achieve the desired political objectives.

Therefore, the findings of this thesis indicate that not only must stronger sanctions be adopted and enforced—specifically ones that virtually embargo Iranian oil; other measures must also be taken to keep these sanctions in place. An embargo (or even partial embargo) on Iranian oil will bring significant instability to world oil markets and will involve significant financial cost to sanctions-participating states, which they must accept. It must also be recognized (by participating sanctioning states) that a humanitarian crisis will develop (as seen in Iraq) due to the conservatives’ and neoconservatives’ economic policy choices. Their propaganda efforts must be effectively countered and the sanctions used in a way to confer legitimacy to the reformist actors in the Iranian political economy. Other efforts to harness global trade to strengthen the reformist actors’ economic base must also be successfully calculated and undertaken. Until these additional measures are undertaken, the ultimate goals of Iranian sanctions will remain elusive and the Iranian enrichment policy will not change.

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